

CENTRAL BANK OF ICELAND



2020

ANNUAL REPORT

- Symbols:**
- * Preliminary or estimated data.
 - 0 Less than half of the unit used.
 - Nil.
 - ... Not available.
 - . Not applicable.

Icelandic letters:

ð/Ð (pronounced like th in English this)

þ/Þ (pronounced like th in English think)

In this report, ð is transliterated as d and þ as th in personal names, for consistency with international references, but otherwise the Icelandic letters are retained.

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Table of Contents

I	Objectives and policy	5
II	Monetary policy	7
	Developments in inflation, interest rates, and exchange rate in 2020	7
	The Monetary Policy Committee	9
	Decisions of the Monetary Policy Committee 2020	9
III	Financial stability	11
	Developments in financial stability	12
	Financial Stability Committee	13
IV	Financial supervision	15
	Financial Supervision Committee	15
	Supervision of financial institutions	15
	Supervision of insurance activities	16
	Supervision of pension funds and third-pillar pension savings custodians	17
	Supervision of markets and business conduct	17
	On-site inspections	18
	Suitability assessments, qualifying holdings, and operating licences	18
	Measures to combat money laundering and terrorist financing	18
	Cases concluded with penalties in 2020	19
V	Other tasks	21
	International reserves	21
	Government debt management	23
	International co-operation	25
	Cash	26
	Jóhannes Nordal cultural heritage grants	27
VI	Management, organisation, and human resources	29
	Governors	29
	Supervisory Board	29
	Organisational structure	29
	Departmental tasks	30
	Central Bank committees	31
	Human resources	32
	Merger of the Central Bank of Iceland and the Financial Supervisory Authority	33
	The impact of COVID-19	33
	Central Bank of Iceland 31 December 2020	33

VII	Operating results and balance sheet	35
	Outlook and capital adequacy criteria	36
VIII	Consolidated Annual Accounts 2020	37
	Profit and Loss Account 2020	43
	Balance Sheet 31 December 2020	44
	Consolidated Statement of Changes in Equity	46
	Consolidated Statement of Cash Flows	47
	Notes	48
	Presentation of profit and loss account and balance sheet	82
IX	Appendix	83
	Press releases from the Central Bank of Iceland 2020	83
	Publications by the Central Bank of Iceland 2020	84
	Central Bank measures in response to COVID-19	85
X	Tables	87
	1 Central Bank interest rates	87
	2 Exchange rate indices	88
	3 Cash issued by the Central Bank at the year-end	88
	4 Summary of the accounts of deposit money banks	89
	5 Summary of the accounts of the banking system	90
	6 Liquidity and reserve ratios in %	91
	7 Main interest rates announced pursuant to Article 10, Paragraph 2, and Temporary Provision III of the Act on Interest and Price Indexation, no. 38/2001	91
	8 Selected annual nominal yields of deposit money banks and penalty rates in % per annum	91
	9 Balance sheet of the Central Bank of Iceland	92
	10 Number of entities regulated by the Financial Supervisory Authority	94
	11 Activities by foreign parties in Iceland	95

Objectives and policy



The Central Bank of Iceland is an independent institution owned by the State and operating under the auspices of the Prime Minister. Its objective is to promote price stability, financial stability, and sound and secure financial activities. The Bank shall also undertake such tasks as are consistent with its role as a central bank, such as maintaining international reserves and promoting a safe, effective financial system, including domestic and cross-border payment intermediation.

The new Act on the Central Bank of Iceland entered into force on 1 January 2020. The main amendments provided for in the new Act pertained to the merger of the Financial Supervisory Authority with the Central Bank. Under the new Central Bank Act, the Bank is responsible for the tasks entrusted by law and Governmental directives to the Financial Supervisory Authority, and the Financial Supervisory Authority is now part of the Central Bank. Furthermore, changes were made to the senior management structure of the Bank, as is described further in Chapter VI. The Bank is also required under the Act to promote the implementation of the Government's economic policy as long as it does not consider such policy inconsistent with the Bank's objectives.

Monetary policy

With the approval of the Minister, the Central Bank may declare a quantitative target for inflation. According to the joint declaration¹ issued by the Government of Iceland and the Central Bank of Iceland on 27 March 2001, the Bank shall aim at a rate of inflation, measured as the twelve-month increase in the consumer

price index (CPI), of as close to 2½% as possible. The Act on the Central Bank of Iceland grants the Bank full independence in conducting monetary policy so as to achieve the Bank's price stability objective.

A five-member Monetary Policy Committee (MPC) takes decisions on the application of the Bank's monetary policy instruments. These monetary policy instruments are the Bank's interest rates, transactions with credit institutions other than loans of last resort, minimum reserve requirements, foreign exchange market transactions, and securities transactions aimed at achieving the Bank's price stability objective. Members of the MPC are the Governor (who acts as chair), the Deputy Governor for Monetary Policy, the Deputy Governor for Financial Stability, and two external members.

Financial stability

The Financial Stability Committee, established in accordance with the provisions of the new Central Bank Act, is tasked with taking decisions on the application of the Bank's financial stability policy instruments. The tasks of the Financial Stability Committee are to assess developments and prospects for the financial system, systemic risks, and financial stability; to define and discuss the measures deemed necessary at any given time to affect the financial system so as to strengthen and preserve financial stability, and submit comments to the relevant authorities when warranted; to approve Government directives and take decisions with which the Committee is entrusted by law, including rules on capital buffers and loan-to-value ratios; and to determine which supervised entities, infrastructure elements, and markets shall be designated as systemically important and of such a nature that their activities could affect financial stability.

¹ The declaration was published in *Monetary Bulletin* 2001/2 and on the Bank's website. Minor changes were made to it in November 2005.

Members of the Committee are the Governor (who acts as chair), the three Deputy Governors, and three external members. The Permanent Secretary or an appointed official from the Ministry responsible for financial stability shall also participate in Committee meetings as a non-voting member with the right to address the meeting and present proposals.

Financial Supervision

A Financial Supervision Committee (FMEN) was established in accordance with the provisions of the new Central Bank Act. The FMEN takes decisions entrusted to the Central Bank Financial Supervisory Authority (FSA Iceland) by law and Governmental directives and is authorised to entrust the Deputy Governor for Financial Supervision with taking non-major decisions.

As is provided for in the Act on the Central Bank, the Committee is chaired by the Governor or the Deputy Governor for Financial Supervision, depending on the agenda. When the FMEN takes decisions on the adoption of rules of procedure and on the transfer of authority to the Deputy Governor for Financial Supervision, as well as decisions pertaining to systemically important financial institutions' capital, liquidity, and funding, the Governor takes a seat on the FMEN as its chair and the Deputy Governor for Financial Supervision acts as vice-chair.

In other instances, the Deputy Governor for Financial Supervision chairs the Committee and the Deputy Governor for Financial Stability acts as vice-chair. The FMEN also has three external members who are experts in matters relating to the financial market.

Other tasks

Other legally mandated tasks entrusted to the Central Bank are discussed elsewhere in this report.

Monetary policy

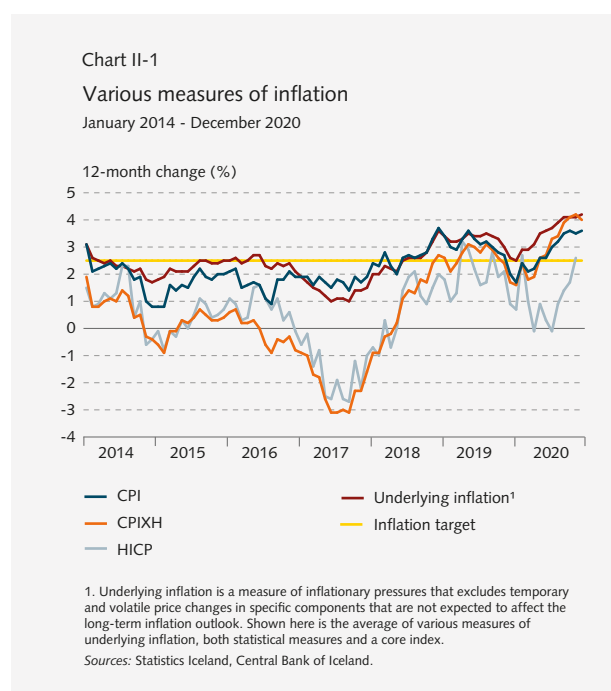


The Central Bank of Iceland is required by law to promote price stability. According to the joint declaration issued by the Central Bank and the Government on 27 March 2001, the objective of price stability is defined as a 2½% rise in the consumer price index (CPI) over a twelve-month period. The Act on the Central Bank of Iceland also stipulates that the Monetary Policy Committee (MPC) shall take decisions on the application of the Bank's monetary policy instruments with the aim of achieving this objective, based on detailed analysis of economic developments and prospects.

Developments in inflation, interest rates, and exchange rate in 2020

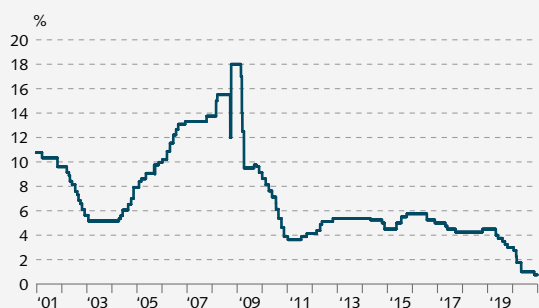
Inflation measured 2.8% in 2020, as compared with 3% in 2019. Inflation was at target in H1/2020 but rose as the year progressed, to 3.6% by December. Inflation excluding housing measured 3% in 2020, and the spread between inflation including and excluding housing widened over the course of the year. Underlying inflation also rose during the year, measuring 4.2% in December 2020, as compared with 2.6% a year earlier.

Imported goods prices were the main driver of inflation in 2020, owing to the depreciation of the króna after the COVID-19 pandemic reached Iceland in late February. Higher prices of various imported goods – such as furniture, housewares, electronic equipment and clothing – affected the CPI most strongly in H2. This item as a whole had risen by 6.3% since December 2019. Domestic goods prices rose as well, by 5.9% year-on-year, led by food and imported input prices. Furthermore, house prices were up 7.8% year-on-year in December, as compared with 4.3% a year earlier.



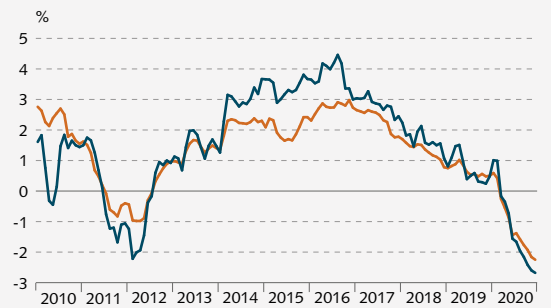
In February 2020, the MPC lowered the Bank's interest rates by 0.25 percentage points. In March, the MPC cut rates twice, by a combined 1 percentage point, and in May it lowered them by a further 0.75 percentage points. In August and October, the Committee decided to hold rates unchanged, but in November it lowered them by another 0.25 percentage points. At the end of 2020, the Bank's key interest rate (the rate on seven-day term deposits) was 0.75% and had been lowered by 2.25 percentage points over the course of the year. The rationale for the February rate cut was that the GDP growth outlook had deteriorated because of headwinds in export sectors and worsening financing terms faced by domestic firms. From March onwards, interest rates were lowered

Chart II-2
Central Bank of Iceland key interest rate¹
Daily data 3 January 2001 - 31 December 2020



1. The Central Bank's key interest rate is defined as follows: the 7-day collateralised lending rate (until 31 March 2009), the rate on deposit institutions' current accounts with the Central Bank (1 April 2009 - 30 September 2009), the average of the current account rate and the rate on 28-day certificates of deposit (1 October 2009 - 20 May 2014), and the rate on 7-day term deposits (from 21 May 2014 onwards).
Source: Central Bank of Iceland.

Chart II-3
Real Central Bank of Iceland interest rates¹
January 2010 - December 2020



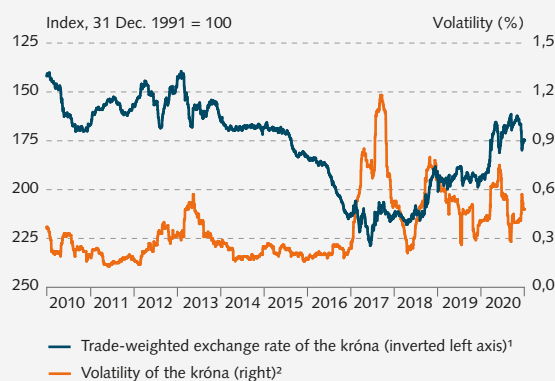
1. From 2010 to May 2014, the nominal policy rate was the average of the current account rate and the maximum rate on 28-day CDs. From May 2014, the policy rate has been the seven-day term deposit rate. 2. Until January 2012, according to twelve-month inflation, one-year business inflation expectations, one-year household inflation expectations, the one-year breakeven inflation rate, and the Central Bank forecast of twelve-month inflation four quarters ahead. From February 2012 onwards, according to the above criteria, plus one-year market inflation expectations based on a quarterly Central Bank survey.
Sources: Gallup, Statistics Iceland, Central Bank of Iceland.

in response to the bleaker outlook due to the pandemic and in an attempt to support an economic recovery.

The monetary stance eased in 2020, with nominal interest rate cuts and other measures aimed at supporting demand and access to credit and preserving financial stability. In March the MPC decided to lower deposit institutions' average reserve requirements, thereby easing their liquidity position and giving them greater scope to respond to the ongoing crisis. Then, in May 2020, the Bank began buying Treasury bonds in order to ensure that the more accommodative monetary stance would be transmitted normally to households and businesses. That same month, the Committee decided to stop offering one-month term deposits so as to increase liquidity in circulation and further strengthen monetary policy transmission. In terms of the average of various measures of inflation and inflation expectations, the Bank's real rate was -2.3% at the end of the year, as compared with 0.6% a year earlier. The real rate in terms of twelve-month inflation fell by 1.2 percentage points over the same period, to -2.8% at the end of the year.

The króna began to depreciate in late February 2020, after the COVID-19 pandemic arrived in Iceland. Shocks to the tourism industry and other export sectors probably weighed heaviest in the depreciation of the króna. During the month of May, the króna appreciated again, reflecting greater optimism about increased tourist numbers and successful public health measures. That appreciation reversed quickly, however, and the króna was under downward pressure from June onwards, although it eased when the Bank announced on 9 September that it would begin a regular currency sales programme. By then, the króna had depreciated by

Chart II-4
Exchange rate and volatility of the króna
Daily data 4 January 2010 - 31 December 2020



1. Price of foreign currency in terms of the króna. Inverted axis shows a stronger króna as a rise. 2. Volatility is measured by the standard deviation of daily changes in the past 3 months.
Source: Central Bank of Iceland.

nearly 16% year-to-date in trade-weighted terms. The aim of the currency sales programme was to deepen the market and improve price formation. The króna began to appreciate after the announcement was made, and it rose still further in November, with the release of news reports on the development of COVID-19 vaccines. By the end of the year, the króna had depreciated by 10.4% in trade-weighted terms, as compared with a depreciation of 3.1% in 2019.

In accordance with its declared policy of intervening in the foreign exchange market to mitigate volatility as it deemed warranted, the Central Bank also traded

in the interbank foreign exchange market. The Bank bought currency for 11.7 b.kr. and sold it for 144.4 b.kr., including 37 b.kr. through the regular sales programme. The Bank's transactions accounted for 37% of interbank market turnover in 2020, as compared with 8% in 2019. Total turnover in the market rose by 120% relative to 2019.

Nominal Treasury bond yields rose temporarily in March 2020, in the wake of news about the Treasury's increased financing need. The rise in yields reversed, however, after the MPC announced the Bank's intention to begin buying Treasury bonds in the secondary market. Yields on most nominal Treasury bonds lay in the 1.0-3.2% range at the end of the year, a decline of as much as 2 percentage points since year-end 2019. Indexed long-term rates also declined early in the year but began to rise in H2. The yield on the longest indexed Treasury bonds was about 0.9% at the year-end, some 0.4 percentage points lower than it had been a year earlier.

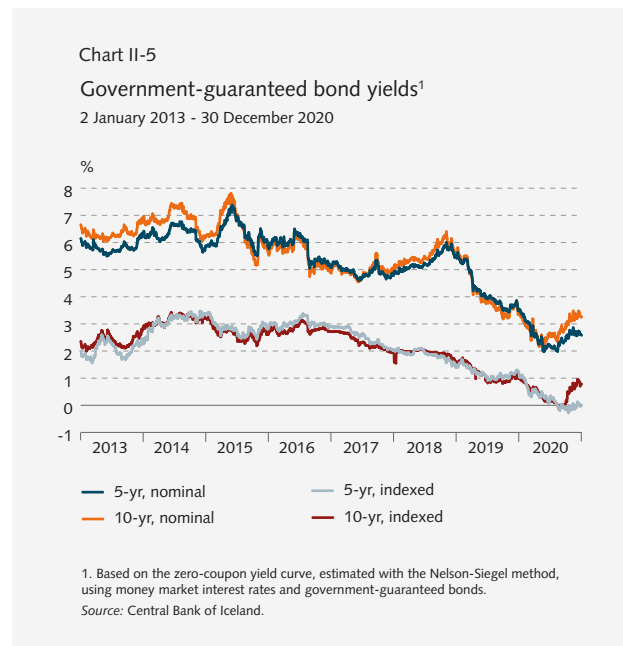
To pursue forward-looking monetary policy, a central bank needs models for assessing the economic outlook, especially inflation. The Bank is constantly developing models for use in assessing the economic outlook and analysing the impact of monetary policy. As an element in this, the Bank publishes its main forecasting model and database on its website.

Further discussion of developments in monetary policy, exchange rate and currency matters, and the Bank's policies and actions in these areas during the year can be found in the minutes of MPC meetings and in the Bank's quarterly *Monetary Bulletin*.

The Monetary Policy Committee

Since the beginning of 2020, when the new Act on the Central Bank entered into force, the MPC has been structured in a new way. According to the new Act, the MPC comprises the Governor, Deputy Governor for Monetary Policy, Deputy Governor for Financial Stability, and two external members. In 2020, MPC members were Governor Ásgeir Jónsson, who chairs the Committee by law; Rannveig Sigurdardóttir, Deputy Governor for Monetary Policy and Deputy Chair of the Committee; Gunnar Jakobsson, Deputy Governor for Financial Stability; Gylfi Zoëga, professor at the University of Iceland; and Katrín Ólafsdóttir, Associate Professor at Reykjavík University.

With the new Central Bank Act, the MPC is now required to hold at least six regular meetings per year instead of the previous eight. The Committee met ten times in 2020, including four extraordinary meet-



ings, and issued a statement on its decision after each one. Furthermore, two weeks after each meeting the Committee published the minutes of its meetings, containing the rationale for its decisions and the assumptions on which they were based. The minutes included the Committee's assessment of economic and monetary developments and prospects, the rationale for members' position, and information on individual members' votes. As is provided for by law, the MPC reported to Parliament on its activities twice during the year.

Decisions of the Monetary Policy Committee in 2020

The MPC's decisions on the application of the Bank's monetary policy instruments were as follows:

5 February: The Governor proposed that the Bank's interest rates be lowered by 0.25 percentage points. Ásgeir Jónsson, Rannveig Sigurdardóttir, and Katrín Ólafsdóttir voted in favour of the proposal. Gylfi Zoëga voted against the Governor's proposal, preferring to keep interest rates unchanged.

11 March: The Governor proposed that the Bank's interest rates be lowered by 0.5 percentage points. All Committee members voted in favour of the proposal. Furthermore, the Committee decided to lower deposit institutions' average reserve requirement from 1% to 0% and hold the fixed reserve requirement at 1%. The Governor also stated that, based on the authorisation provided for in liquidity rules, the Bank would designate deposits held in fixed reserve accounts with the Central

Bank by entities subject to reserve requirements as high-quality liquid assets. The fixed reserve requirement could thereby be considered a liquidity buffer according to liquidity rules.

18 March (extraordinary meeting): The Governor proposed that the Bank's interest rates be lowered by 0.5 percentage points. All Committee members voted in favour of the proposal.

23 March (extraordinary meeting): The Governor proposed that the Bank begin direct purchases of Treasury bonds in the secondary market. All members voted in favour of the proposal. The Governor proposed thereafter that the Bank be authorised to purchase Treasury bonds for up to 150 b.kr., or about 5% of GDP. All members voted in favour of the proposal.

8 April (extraordinary meeting): The Governor requested the Committee's approval of the Bank's establishment of a special temporary collateralised lending facility and a temporary expansion of the list of collateral deemed eligible for Central Bank facilities for financial institutions. All members approved the measure.

20 May: The Governor proposed that the Bank's interest rates be lowered by 0.75 percentage points. The Governor also proposed that the Bank stop offering one-month term deposits. All Committee members voted in favour of both proposals.

24 June (extraordinary meeting): At a joint meeting of the Monetary Policy Committee and the Financial Stability Committee, the Governor proposed that, because of the uniqueness of support loans bearing a 100% Treasury guarantee and the circumstances prevailing due to the pandemic, the Central Bank should develop a separate temporary collateralised lending framework for support loans, subject to the terms offered at any given time on seven-day term deposits with the Central Bank. All members voted in favour of the proposal.

26 August: The Governor proposed that the Bank's interest rates be held unchanged. All Committee members voted in favour of the proposal.

7 October: The Governor proposed that the Bank's interest rates be held unchanged. All Committee members voted in favour of the proposal.

18 November: The Governor proposed that the Bank's interest rates be lowered by 0.25 percentage points. All Committee members voted in favour of the proposal.



Monetary Policy Committee 2020. From left are Rannveig Sigurdardottir, Deputy Governor for Monetary Policy, Deputy Chairman; Gylfi Zoëga, Professor University of Iceland; Ásgeir Jónsson Governor, Chairman; Katrín Ólafsdóttir, Assistant Professor Reykjavik University; and Gunnar Jakobsson, Deputy Governor for Financial Stability.

Financial stability



One of the Central Bank of Iceland's tasks is to promote financial stability. Financial stability means that the financial system is resilient enough to withstand shocks to the economy and financial markets, to mediate credit and payments, and to redistribute risks appropriately.

The Bank analyses and monitors the position of the financial system and payment intermediation and responds as needed to counteract developments that could undermine the stability of the system. The Bank also closely monitors individual credit institutions, financial markets, households and businesses, the external position of the economy, capital flows, and the refinancing risk faced by domestic participants in foreign credit markets. By law, the Central Bank Financial Stability Committee (FSN) takes decisions on the application of the Bank's policy instruments in order to ensure and preserve financial stability.

The Central Bank is tasked with enforcing the Foreign Exchange Act, no. 87/1992, and rules set on the basis of the Act, including the Rules on Foreign Exchange Balance, no. 784/2018. The Bank conducts general and targeted monitoring of compliance with the Foreign Exchange Act and related rules, and it provides guidance and instruction in this context. As regards foreign exchange matters, the year was affected by projects involving the liberalisation of the remaining capital controls. Among these projects was the comprehensive review of legislation and rules on foreign exchange, as well as supervision of the special reserve requirement (capital flow management measure) and the Act on the Treatment of Króna-Denominated Assets Subject to Special Restrictions, no. 37/2016. At the end of 2020, the stock of offshore krónur as defined in Act no. 37/2016 came to 26.6 b.kr. (0.9% of GDP), down

from 59.1 b.kr. (about 2% of GDP) at the beginning of the year.

The Central Bank's goal is to promote security, efficiency, and efficacy of core infrastructure in the Icelandic financial system – i.e., systemically important financial market infrastructure – thereby safeguarding financial stability. Work was done during the year towards the preparation and launch of new core infrastructure elements. These included, on the one hand, the new Nasdaq CSD securities settlement system, which was brought into use in August, after Nasdaq CSD Iceland merged with Nasdaq CSD SE, and on the other, the Central Bank's new interbank system, which was launched in late October. An extensive contingency exercise was held during the run-up to the interbank system launch, and wide-ranging communication was held with various parties, partly to collect information for an assessment relating to the Bank's recommendation that the Minister of Finance and Economic Affairs recognise the aforementioned systems in accordance with Act no. 90/1999. During the year, participation agreements for the Bank's new interbank system were renewed, and rules were adopted for the system's operations.

In 2019, the Bank's rules on credit institutions' liquidity ratios were amended to include a new 50% minimum liquidity ratio in Icelandic krónur. The plan was to provide for a two-year adaptation period, so that the minimum ratio would be 30% in 2020 and 40% in 2021. In 2020, the adaptation period was extended by one year; therefore, the ratio will be 30% through end-2021 and 40% through end-2022, and the 50% ratio will take effect at the beginning of 2023.

The Act on Recovery and Resolution of Credit Institutions and Investment Firms, no. 70/2020, entered

into force on 1 September 2020. The Act entrusts powers of resolution to the Central Bank, which entails the authority to take decisions on resolution and to apply resolution measures in the case of a financial undertaking that cannot honour its obligations or is unlikely to be able to. According to Article 4 of the Act, the Central Bank of Iceland Resolution Authority shall be separate from other activities within the Bank's organisational structure, particularly the Financial Supervisory Authority (FSA Iceland). The Central Bank's Resolution Authority formally commenced operation in November 2020.

The Resolution Authority prepares a resolution plan for each financial institution that could potentially affect financial stability if it were to become insolvent. The resolution plans, which will only be accessible to the Resolution Authority itself, will be prepared based on information from FSA Iceland and the undertakings concerned. They are based on a strategic business analysis that entails an overview of all important and necessary activities of financial institutions. The resolution plans shall lay down the optimum resolution policy and specify the action the Resolution Authority will take in the event that the prerequisites for resolution apply to a given institution.

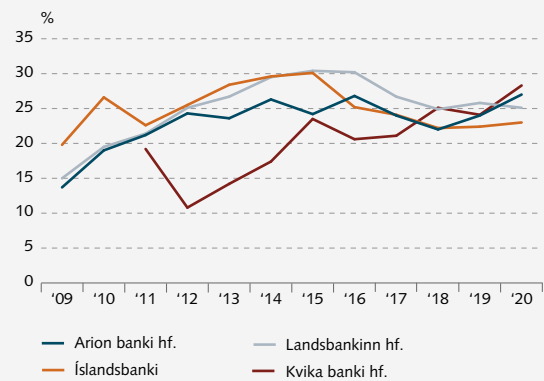
Developments in financial stability

Risk increased in the financial system in 2020, primarily because of the pandemic. International air travel virtually halted, and the necessary public health measures imposed by the authorities had a pronounced negative impact on various types of domestic services. As a result, activity in the tourism industry and related services sectors contracted abruptly at the end of Q1/2020.

The Government adopted a variety of measures to address firms' revenue losses and the surge in unemployment, including revenue loss subsidies, resilience subsidies, and closure subsidies; support loans and supplemental loans; and part-time unemployment benefits. Furthermore, the Central Bank supported households and businesses by lowering interest rates. Central Bank measures to boost financial system liquidity, together with the suspension of the countercyclical capital buffer, made it easier for financial institutions to maintain their lending capacity and offer borrowers moratoria on payment.

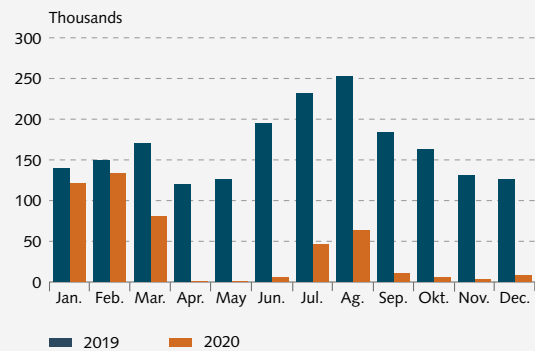
Iceland's financial institutions were strong at the end of 2020. The commercial banks' capital and liquidity positions were well above Central Bank requirements, and all of the banks operated at a profit during the year, in spite of a considerable increase in impairment.

Chart III-1
Commercial banks' capital adequacy ratios¹



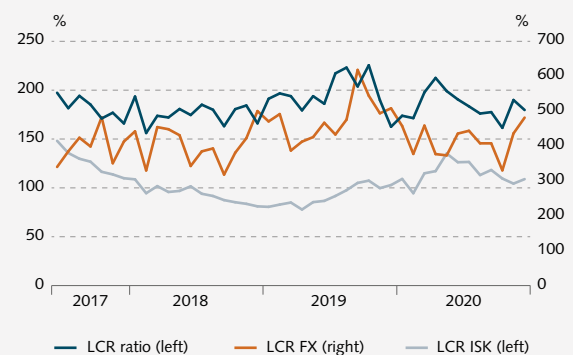
1. Consolidated figures. Capital base as % of risk-weighted base.
Sources: Commercial banks' annual accounts.

Chart III-2
Tourist departures via Keflavík Airport



Sources: Icelandic Tourist Board, Isavia.

Chart III-3
The three large commercial banks' liquidity coverage ratio¹



1. Consolidated figures.
Source: Central Bank of Iceland.

Streamlining measures undertaken by the banks have lowered costs and strengthened their core operations, even though interest rate differential declined because of lower interest rates.

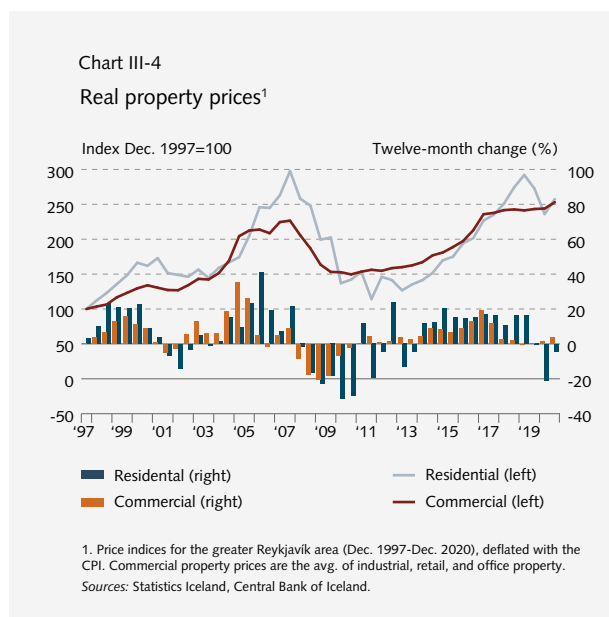
Banking system lending grew somewhat in 2020, as is reflected in increased household indebtedness following interest rate cuts and a shift in the credit stock from other lenders. There was a small contraction in corporate lending during the year. Non-performing loan ratios changed little during the year, although a portion of loans were protected by special measures, particularly loans to companies in tourism and other services. Among households, however, there was little demand for the measures.

The terms available to the banks in foreign credit markets deteriorated markedly early in the pandemic but improved again at the beginning of summer. By the end of 2020, they were about the same as at the start of the year. As a result, the banks had ready access to liquidity in both krónur and foreign currencies by the year-end. The banks paid no dividends in 2020, as the Central Bank had encouraged their boards of directors to postpone dividend payments in order to shore up resilience and support the banks' capital ratios while the economic impact of the pandemic was still unknown. The Icelandic banks' capital and leverage ratios are very high in international context.

Although uncertainty and risk in the financial system increased in 2020, the Bank's Financial Stability Committee noted in its December statement that cyclical systemic risk had not increased materially.

Financial Stability Committee

By law, the Central Bank Financial Stability Committee (FSN) takes decisions on the application of the Bank's financial stability policy instruments. The FSN is tasked with assessing developments and prospects for the financial system, systemic risk, and financial stability. Furthermore, the FSN is tasked with discussing and defining the actions deemed necessary at any given time in order to affect the financial system so as to strengthen and preserve financial stability, and to this end, the Committee is required to direct comments to the appropriate Governmental authorities when warranted. The FSN is also required to approve Governmental directives and take the decisions entrusted to it by law. Moreover, it shall decide which supervised entities, infrastructure elements, and markets shall be considered systemically important and of such a nature that their activities could affect financial stability.



The work and decisions of the Financial Stability Committee

Members of the Financial Stability Committee are Governor Ásgeir Jónsson, who acts as chair; Gunnar Jakobsson, Deputy Governor for Financial Stability and deputy chair; Rannveig Sigurdardóttir, Deputy Governor for Monetary Policy; Unnur Gunnarsdóttir, Deputy Governor for Financial Supervision; Axel Hall, Assistant Professor at Reykjavík University; Bryndís Ásbjarnardóttir, economist at Statistics Iceland; and Gudmundur Kristján Tómasson, former Director of Financial Market Infrastructure at the Central Bank of Iceland. In addition, a representative from the Ministry of Finance and Economic Affairs attends Committee meetings, with the right to address the meeting and present proposals.

The Financial Stability Committee is required by law to meet at least four times a year. The Committee met six times in 2020. The FSN's extra meetings were held because of the need to set rules of procedure during the Committee's first year of operation and because of COVID-19 and responses to the repercussions of the pandemic.

At the first meeting, held on 10 March 2020, the Committee adopted rules of procedure, as is stipulated in the Central Bank Act, and discussed the changes in the economic outlook due to the pandemic. The Government's initial responses to the pandemic were presented at the meeting.

At its second meeting, held on 16 March, the Committee decided to lift the 2% countercyclical capital buffer that had been imposed on financial institutions. It also decided not to increase the countercyclical capital

buffer again in the coming twelve months, thereby holding it unchanged according to the relevant rules until at least Q1/2022.

At its third meeting, held on 31 March, the FSN completed its review of the capital buffers for systemic risk and systemic importance, deciding to hold both buffers unchanged. It was also decided that the three large commercial banks would retain their designation as systemically important institutions. The Committee also recommended to the Governor that a special temporary loan facility be established for financial institutions.

At the fourth meeting, on 22 and 23 June, the FSN decided to hold the countercyclical capital buffer unchanged. After this meeting, part of which was a joint meeting of the Financial Stability Committee and the Monetary Policy Committee, the two committees published a joint announcement about a special temporary collateralised framework for support loans. The FSN agreed at its meeting that the Central Bank should develop such a framework to finance support loans bearing a 100% Treasury guarantee.

At its fifth meeting, held on 21 and 22 September, the Committee decided to keep the countercyclical capital buffer unchanged.

At its sixth and last meeting in 2020, held on 14 and 15 December, the FSN decided to designate the Central Bank's new interbank system and Nasdaq CDS SE's securities settlement system as systemically important financial market infrastructure elements. It also decided to hold the countercyclical capital buffer unchanged at 0%.

The Committee made its decisions public by issuing a statement after each meeting, thereby explaining the application of financial stability policy instruments and presenting its assessment of developments and prospects for the financial system, systemic risk, and financial stability. The minutes of FSN meetings are made public. Further information can be found in the report *Financial Stability*, which was published twice in 2020.



Financial Stability Committee, 2020. Front row, from left: Rannveig Sigurdardóttir, Deputy Governor for Monetary Policy; Ásgeir Jónsson, Governor, chair; Gunnar Jakobsson, Deputy Governor for Financial Stability, vice-chair; and Unnur Gunnarsdóttir, Deputy Governor for Financial Supervision. Back row, from left: Tómas Brynjólfsson, Director General, Ministry of Finance and Economic Affairs, with the right to address the meeting but without voting rights; Bryndís Ásbjarnardóttir, Economist, Statistics Iceland; Gudmundur Kristján Tómasson, former Director of Financial Market Infrastructure, Central Bank of Iceland; and Axel Hall, Assistant Professor, Reykjavík University.

Financial supervision

IV

The Central Bank of Iceland is tasked with promoting sound and secure financial activities. The Central Bank is responsible for the tasks entrusted by law and Governmental directives to the Financial Supervisory Authority (FSA Iceland). The Bank monitors supervised entities to ensure that their activities are in compliance with law and Governmental directives, and that they are in other respects consistent with sound and appropriate business practice; cf. the Act on Official Supervision of Financial Activities. The Bank also ensures that supervised entities are attentive to consumer protection in their activities.

Financial Supervision Committee

The Financial Supervision Committee (FMEN) takes decisions entrusted to the Financial Supervisory Authority by law or Governmental directives. The Committee is authorised to entrust the Deputy Governor for Financial Supervision with taking non-major decisions.

In 2020, the FMEN held ten meetings, in addition to handling nine cases outside meetings, as it is authorised to do.

Members of the FMEN are Governor Ásgeir Jónsson, Unnur Gunnarsdóttir, Deputy Governor for Financial Supervision, who acts as chair; Gunnar Jakobsson, Deputy Governor for Financial Stability and vice-chair; economist Ásta Thórarinsdóttir; Andri Fannar Bergthórsson, Assistant Professor at Reykjavík University; and Gudrún Thorleifsdóttir, Director General at the Ministry of Finance and Economic Affairs. As is provided for in the Act on the Central Bank, the Committee is chaired by the Governor or the Deputy Governor for Financial Supervision, depending on the agenda. When

the FMEN takes decisions on the adoption of rules of procedure and on the transfer of authority to the Deputy Governor for Financial Supervision, as well as decisions pertaining to systemically important financial institutions' capital, liquidity, and funding, the Governor takes a seat on the FMEN as its chair and the Deputy Governor for Financial Supervision acts as vice-chair.

In other instances, the Deputy Governor for Financial Supervision chairs the Committee and the Deputy Governor for Financial Stability acts as vice-chair.

Supervision of financial institutions

The Central Bank's supervision of financial institutions includes supervision of commercial banks, savings banks, credit institutions, investment firms, payment institutions, and electronic money institutions.

Regular supervision of financial institutions was carried out in accordance with FSA Iceland's risk-based supervision model, which defines the frequency with which key risk factors in the institution's operations are examined. It entails a review of data and supervisory reports submitted by the institutions concerned, as well as examination of key indicators. Data are gathered on the financial markets, based on European technical standards and Icelandic reports. The data collected pertain in particular to operations, financial statements the main risks they are exposed to e.g. financial institutions' loan portfolios, own funds, liquidity and funding and information on asset quality.

The COVID-19 pandemic and associated response measures affected the supervision of financial institutions' activities during the year. At the beginning of the pandemic, the European Banking Authority (EBA) and other European supervisory bodies encouraged credit

institutions to use the regulatory scope available to them in order to mitigate the procyclical impact of the pandemic on the economy, as it is important that households and businesses have ready access to financing.

Domestic credit institutions granted broad general moratoria on payment in order to support firms and individuals on the basis of an agreement among the institutions concerned, which was signed in late March 2020. In summer 2020, nearly 13% of all loans granted by the domestic systemically important banks (D-SIB) were protected by moratoria, although the percentage declined rapidly over the course of the year.

Loans in moratorium were generally classified as performing at the end of 2020, in accordance with guidelines issued by the EBA in response to the spread of the pandemic. There are signs of a marked increase in corporate loans classified as forborne since the general moratorium period ended. These are loans to financially distressed firms that have been granted concessions such as extended moratoria.

Operational risk was assigned greater weight in the risk assessments carried out during the year, owing to increased teleworking in the wake of the pandemic and stronger emphasis on pandemic-related monitoring. The impact of the pandemic on financial institutions' staffing levels was examined, as were the ways in which institutions' contingency plans were used in response to the pandemic. Financial institutions' cybersecurity measures were examined as well, with emphasis on defences due to telework and new digital solutions.

Supervisory review and evaluation process (SREP)

The SREP assessments for the three D-SIBs had already begun by the time the COVID-19 pandemic reached Iceland in early 2020. The FMEN issued a statement in April 2020, announcing that the SREP was in progress and noting that in view of the ongoing economic difficulties, final decisions on capital requirements would probably be based on financial statements later in 2020 rather than at the end of 2019. Furthermore, no supervisory stress tests would be conducted at that time in connection with the SREP.

In September 2020, the FMEN committee decided that the results of the 2019 SREP assessment concerning additional capital requirements (Pillar II-R) would remain unchanged and that close monitoring of key risks in the banks' operations would continue. The additional capital requirement would be reviewed if needed, and no later than during the 2021 SREP. The FMEN also decided in March 2020 to lower the countercyclical capital buffer from 2% to 0%.

In addition to assessing the need for additional capital requirements, the SREP entails a review of factors such as business model viability and sustainability, internal governance and institution-wide controls, operational risk, credit risk, concentration risk, market risk and interest rate risk in the banking book (IRRBB), and liquidity and funding risk, including the management and control of these risks. Even though it has been decided that the additional capital requirements will remain unchanged, comments and suggestions on the above-mentioned factors were communicated formally to the banks in late 2020.

Recovery plans

At the end of 2020, the D-SIBs submitted recovery plans for the third time. The plans will be reviewed in 2021. Other less significant financial institutions submitted simplified recovery contingency plans for the first time in October 2020.

Supervision of insurance activities

Regular monitoring of insurance undertakings was carried out in accordance with FSA Iceland's basic supervision model, which defines the frequency with which key risk factors in the undertakings' operations are examined.

It entailed a review of the undertakings' own risk and solvency assessment (ORSA) and interviews with specified key employees. Proactive checks were carried out at insurance undertakings, where the boards of directors' self-assessments were examined and the procedure for investing in specialised and/or unlisted assets reviewed.

Insurance undertakings are required to publish a solvency and financial condition report (SFCR) and submit a regular supervisory report (RSR) to FSA Iceland. These reports are an element in the harmonised Pillar 3 reporting requirements provided for in the Solvency II directive. In 2020, FSA Iceland reviewed individual chapters of the reports and gave feedback to the insurance companies concerned. Selected parts of the solvency requirement calculations were examined as well.

FSA Iceland also participated in gathering information for the European Insurance and Occupational Pensions Authority's (EIOPA) consultation with the European Commission in connection with the review of Solvency II. This information gathering is an element in assessing the impact EIOPA's recommendations have on insurance undertakings' solvency.

Activities in the insurance market were monitored closely in connection with COVID-19. Because of uncertainty about the short- and long-term impact of the pan-

demic, FSA Iceland encouraged insurance companies to adopt appropriate measures to shore up their resilience.

Supervision of pension funds and third-pillar pension savings custodians

Regular monitoring of pension funds was carried out in accordance with FSA Iceland's basic supervision model, which defines the frequency with which key risk factors in the funds' operations are examined. Regular supervision includes monitoring the pension funds' compliance with regulatory provisions. During the review, it emerged that four funds had violated their investment authorisations. Furthermore, special monthly data collection was carried out due to the COVID-19 pandemic.

The funds' own risk self-assessments (ORAs) were reviewed, and interviews were conducted with specified key employees. FSA Iceland also examined specified pension funds' investment procedures. Emphasis was placed on examining how decisions and follow-up were handled, and whether the funds had documented their investment procedures for specialised investments in a satisfactory manner. Furthermore, the Authority reviewed the mechanisms under which the boards, investment committees, and risk management departments of the pension funds participated in and supervised the investment process.

FSA Iceland placed strong emphasis on pension funds' governance practices in its work during the year, including examining the supervisory role of their boards of directors; communications between the board, on the one hand, and the risk officer and internal auditor, on the other; and the boards' self-assessments. In several instances, the board's involvement in decisions on specific investments was examined, as were the associated governance practices.

The activities of pension funds were monitored closely in connection with COVID-19. Pension funds and third-pillar pension savings custodians adapted their operations to a changed work environment so as to minimise disruption of service to fund members.

Supervision of markets and business conduct

Supervision of the securities market and business conduct was affected by the COVID-19 pandemic in many ways during the year. In addition to the changes in the work environment, the pandemic led to increased reporting to the European Securities and Markets Authority (ESMA). In addition, the pandemic has had a discernible impact

on securities issuers in the areas covered by FSA Iceland's reviews.

Supervision of the securities market

Of the cases relating to the securities market that were examined during the year, 33 were concluded, the vast majority with no further action taken, although a few were concluded with comments, settlements, or fines. Fifteen of the above cases pertained to issuers' information disclosure requirements, nine involved potential insider dealing, five involved potential market abuse, and four fell into other categories.

Among the most extensive tasks in 2020 were the confirmation of prospectuses and supervision of securities offerings, as well as financial supervision of funds for collective investment undertakings and the management companies that operate them. As in previous years, a significant amount of work was done on implementation of new securities market legislation. The number of supervisory tasks increased with the new legislation. In particular, there was an increase in administration and monitoring of reporting by supervised entities, and it was assumed that increased emphasis would be placed on projects related to reporting. Also prominent during the year were tasks relating to monitoring of market participants' conduct, including information disclosure by issuers, market abuse, and insider dealing. The Bank participated actively in international cooperation and was represented on various ESMA committees, as well as the supervisory college that monitors the activities of Nasdaq CSD in Latvia, which handles securities settlement in Iceland and the Baltics. The Bank also had a representative in the supervisory college that monitors the activities of the Nasdaq exchanges in the Nordic region.

In 2020, the Nasdaq CSD Iceland securities depository merged with Nasdaq CSD SE, which is licensed in Latvia and operates Iceland's securities settlement system through a branch. In a comparable way, Nasdaq CSD SE operates securities settlement systems in the Baltic countries.

Cases relating to takeovers of listed companies were far more prominent in 2020 than in previous years.

Supervision of business practices

In monitoring supervised entities' business practices and protecting consumer interests, FSA Iceland carries out proactive checks focusing for example on information disclosure to customers, obligations relating to product sales and distribution, presentation of marketing materials, and requirements regarding internal rules and procedures as these relate to business practices and consum-

ers. Furthermore it does a range of analytical work relating to financial supervision including an ongoing analysis of the investment options available to retail investors.

FSA Iceland receives queries, comments, and complaints from the public concerning supervised entities' business practices, and it provides information and guidance to the parties concerned. Comments on supervised entities' business practices are also very useful in the analysis of potential risks and problems; furthermore, they can result in proactive checks and investigations. In 2020, the Authority received 246 comments pertaining to business practices in the financial market.

On-site inspections

On-site inspections are among the methods FSA Iceland uses to carry out its supervision of regulated entities. The aim of on-site inspections is to analyse risks in supervised entities' activities in detail and evaluate their business plans, governance practices, and internal controls. Decisions about on-site inspections are based on supervised entities' impact category, as well as the results of risk assessments. Supervised entities' size, activities, and risk profile are also taken into account. The COVID-19 pandemic made a strong impact on the on-site inspections planned for the year, in that some of them could not be carried out on the entities premises. Instead, they were conducted in part via remote meetings held with representatives of the entities concerned. Furthermore, it was decided to postpone several inspections that had been planned for 2020, so as to enable the entities in question to concentrate on pressing matters relating to the pandemic.

FSA Iceland completed 18 on-site inspections in 2020. These inspections focused mainly on supervised entities' anti-money laundering and terrorist financing measures, credit risk and operational risk in their activities, and internal control systems.

Suitability assessments, qualifying holdings, and operating licences

Assessment of board members' and managing directors' eligibility

FSA Iceland conducts a suitability-assessment of supervised entities' board members and managing directors; however, the entities concerned are always responsible for ensuring that their board members, managing directors, and key executives satisfy the regulatory suitability requirements. In 2020, the Central Bank conducted fitness and suitability assessment of 105 board mem-

bers and managing directors at supervised entities, the vast majority of them board members. Because of the COVID-19 pandemic, it was not possible to interview all of the board members concerned, and the assessments could not be completed by the year-end. They are scheduled for completion in the first half of 2021, however.

Qualifying holdings

The Central Bank assesses the eligibility of parties intending to acquire qualifying holdings in financial institutions, insurance companies, electronic money institutions, and payment institutions. There were some changes in ownership of financial institutions and other supervised entities in 2020. Notifications of qualifying holdings in six supervised entities were approved during the year.

Operating licences and registrations

There were numerous changes relating to supervised entities' operating licences in 2020. Among new licences granted were one licence for operation as a payment institution, one insurance intermediary licence, two debt collection licences, and two registrations for virtual currency service providers. In addition to these were nine operating licences and seven registrations following the entry into force of new legislation on alternative investment fund managers. One credit institution's licence was revoked, one lender was removed from the register, and one debt collection licence was revoked.

Measures to combat money laundering and terrorist financing

FSA Iceland carries out risk-based supervision of entities subject to notification requirements (obliged entities) in accordance with the Act on Measures Against Money Laundering and Terrorist Financing. There were 82 such obliged entities at the end of 2020, up from 72 a year earlier. FSA Iceland conducted 64 checks on anti-money laundering and terrorist financing measures in 2020, including four on-site investigations. Other checks pertained to compliance with legislation on freezing of funds, in which the Authority examined how supervision of parties on sanctions lists was handled.

In April 2020, FSA Iceland issued guidelines on the COVID-19 pandemic to obliged entities. The guidelines reiterated that the entities concerned should continue their anti-money laundering and terrorist financing measures and be on the watch for new methods and channels for money laundering, owing to the changed economic environment.

In October, the Financial Action Task Force (FATF), an international anti-money laundering and terrorist financing body, removed Iceland from the “grey” list of countries under increased scrutiny due to inadequate measures to combat money laundering and terrorist financing. The decision was made following an on-site investigation that took place in Iceland in September 2020, which confirmed that the Icelandic authorities had completed the measures required for removal from the grey list. The Icelandic Government had been engaged in broad-based reforms of its anti-money laundering architecture since April 2018. The Central Bank and other Governmental authorities will continue to strengthen Iceland’s defences against money laundering and terrorist financing.

Twice during the period of increased scrutiny, surveys were carried out to determine whether the FATF decision had affected supervised entities’ activities and, if so, what impact it had made. It could be inferred from the responses that the FATF decision had made very little impact during the period in question.

Cases concluded with penalties in 2020

In 2020, the FSA Iceland concluded four cases involving violations by reaching a settlement with the parties concerned. The Authority also decided to impose administrative fines in three additional cases. The fines in question, which ranged from 850,000 kr. to 87.7 m.kr., totalled just over 140 m.kr. Fines imposed by the Central Bank revert to the Treasury. In two of these cases, the plaintiffs have referred the imposition of the administrative fines to the courts, demanding that the decisions be invalidated. Penalties are discussed in greater detail in the Bank’s *Financial Supervision* report.

Tables showing the number of parties under supervision by FSA Iceland and the activities of foreign entities in Iceland can be found in tables no. 10 and 11 on page 94 and 95.



Financial Supervision Committee, 2020. Front row, from left: Unnur Gunnarsdóttir, Deputy Governor for Financial Supervision; Ásgeir Jónsson, Governor; and Gunnar Jakobsson, Deputy Governor for Financial Stability. Back row, from left: Guðrún Thorleifsdóttir, Director General, Ministry of Finance and Economic Affairs; Andri Fannar Bergthórsson, Assistant Professor, Reykjavík University; and Ásta Thórarinsdóttir, Economist. Governor Ásgeir Jónsson takes a seat on the FMEN as its chair when the Committee takes decisions on the adoption of rules of procedure and on the transfer of authority to the Deputy Governor for Financial Supervision, as well as decisions pertaining to systemically important financial institutions’ capital, liquidity, and funding. Then, Deputy Governor Unnur Gunnarsdóttir takes the seat of vice-chair. Otherwise, Unnur Gunnarsdóttir is chair and Gunnar Jakobsson vice-chair.

Other tasks



International reserves

Role of the reserves

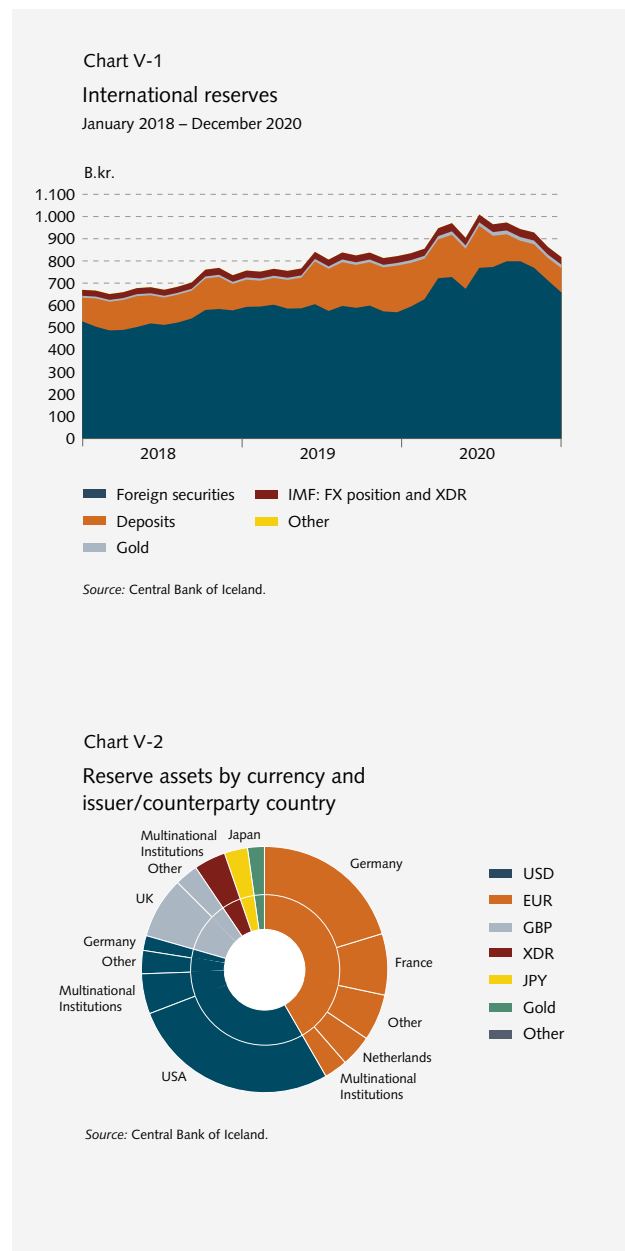
The Central Bank of Iceland maintains international reserves in accordance with its objectives and role as described in Act no. 92/2019. The international reserves are foreign-denominated assets held by the Central Bank: foreign bank deposits, bonds, special drawing rights and deposits with the International Monetary Fund (IMF), gold, and other foreign assets.

The role of the reserves is fourfold: first, to mitigate volatility in Iceland's balance of payments; second, to reduce the likelihood that movement of capital to and from Iceland will compromise financial stability; third, as a part of the Treasury and Central Bank's management of assets and liabilities, so that the Icelandic Government can service its foreign debt, pay foreign expenses, and honour other international obligations; fourth, as a reserve fund that can be tapped in the event of shocks.

At any given point in time, the optimum size of the international reserves is determined by Iceland's external debt, monetary policy, financial system structure and position, scope of international trade, and capital flows to and from the country.

Developments in the reserves in 2020

At the end of 2020, the international reserves totalled 817 b.kr., the equivalent of 6.4 billion US dollars. The reserves had shrunk by 5 b.kr. during the year. The decline was due mainly to foreign exchange market intervention in the amount of 133 b.kr. and payments on Treasury foreign loan in the amount of 2 b.kr. Other foreign exchange market transactions reduced the reserves by 5 b.kr. Also affecting the reserves was the issuance



of a Treasury bond in the amount of 500 million euros in June and the maturity of another eurobond in July, in the amount of 292 million euros. The combined effect of these transactions was to increase the reserves by 30 b.kr.

At the end of the year, the international reserves totalled 28% of GDP and 38% of broad money holdings (M3), and they covered nine months' worth of goods and services imports.

Returns and interest income

Returns on the Bank's foreign exchange reserves were positive in the amount of 105 b.kr. in 2020, owing mainly to the depreciation of the króna. The recognised exchange rate difference was positive by 89 b.kr. Interest income on the reserves was positive by 6 b.kr., and recognised changes in the market value of securities increased the reserves by 10 b.kr. During the year, the return on bonds and deposits was 1.8%, excluding the effects of exchange rate differences.

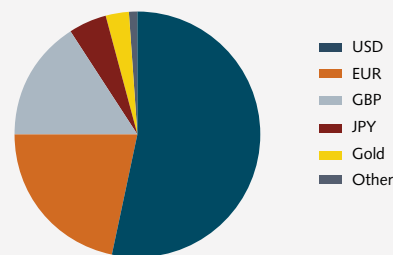
Reserve maintenance

The Rules on Reserve Maintenance are adopted with reference to Article 3, Paragraph 3 and Article 30, Paragraph 1 of Act no. 92/2019 and are set by the Governor and Deputy Governors. The rules contain provisions on key points concerning reserve maintenance, including purpose, structure, investment authorisations, and outside limits of acceptable risk.

In maintaining and investing the international reserves, the Central Bank takes risks that must be managed. The most important risk lies in the possibility that the Bank will be unable to use the reserves to achieve its objectives or carry out its role as a central bank. Foreign exchange risk, on the other hand, is the risk that has the greatest impact on the Bank's balance sheet. The reserves are in foreign currencies, while most of the Bank's liabilities are in Icelandic krónur. As a result, exchange rate movements strongly affect the Bank's income and expenses, as well as the value of assets and liabilities denominated in krónur. Unrealised income and expense, including exchange rate differences, are entered to the value adjustment reserve, and no transfer to the Treasury is made on these items. This is done to prevent payments to the Treasury on profit that may never materialise and could have a strongly negative impact on the Bank's balance sheet over time.

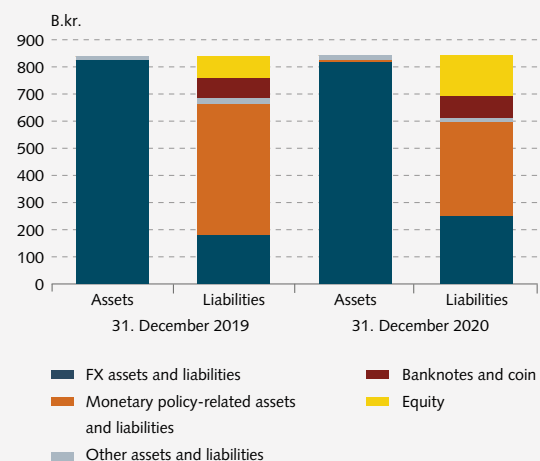
A large share of the international reserves are invested in foreign securities, which accounted for some 80% of the reserves at the end of 2020. Deposits comprised 14% of the reserves, the vast majority of them held in central banks. The Bank's gold holdings, which

Chart V-3
Foreign exchange balance by currency



Source: Central Bank of Iceland.

Chart V-4
Central Bank of Iceland balance sheet



Source: Central Bank of Iceland.

were unchanged year-on-year in volume terms, were valued at 15.4 b.kr., or about 1.9% of the reserves, at the end of 2020. The Bank's foreign exchange balance – i.e., its foreign-denominated assets net of foreign-denominated liabilities – was positive by 572 b.kr., the equivalent of 4.5 billion US dollars, at the end of 2020.

For the purposes of reserve management, highly liquid assets include bonds denominated in US dollars and euros and issued by the state in the state's own currency, and deposits with the central banks in these countries/regions or the Bank for International Settlements. Issuers must have a credit rating of at least AA in order for their securities to be classified as highly liquid assets. Highly liquid assets accounted for 53% of the Central Bank's foreign exchange reserves at the end of 2020.

Chart V-2 gives a breakdown of reserve assets by country and currency as of end-2020. Further discussion of the management of the Bank's financial risk can be found in the notes to the financial statements.

Government debt management

Agreement on Treasury debt management

In accordance with an agreement made with the Ministry of Finance and Economic Affairs, the Central Bank of Iceland oversees Treasury foreign borrowing; conducts domestic auctions, buybacks, and Treasury bond redemptions; executes primary dealer agreements; and oversees securities lending to primary dealers. The Bank handles risk management, debt management, and information disclosure on Treasury debt. Under the agreement, the Bank handles tasks relating to issuance of marketable Treasury securities and Treasury guarantees and relending. The Bank also oversees issuance of bonds for Treasury relending.

Domestic debt management

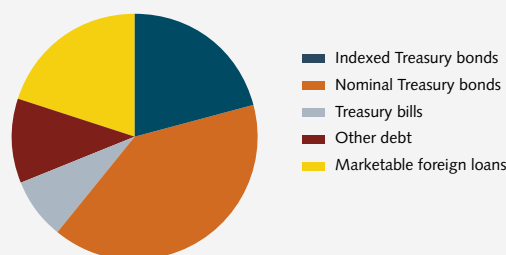
The Government Debt *Prospect* for 2020 assumed that Treasury issuance would total 40 b.kr.; however, the Treasury's financing need grew substantially because of the economic contraction brought on by the COVID-19 pandemic, and five supplementary fiscal budget proposals were introduced in Parliament during the year. At the beginning of the pandemic, the Government decided to bring all of its strength to bear against the disease and its repercussions. The Treasury's estimated financing need soared as a result, and by the end of the year, Treasury issuance totalled 163.5 b.kr. nominal value, or 182.5 b.kr. market value.

Treasury bond series RIKB 20 0205 matured during the year, with an outstanding amount of just under 57 b.kr. Issuance of a new two-year Treasury bond, RIKB 23 0515, was brought forward by one year in response to the increased financing need. The bond was well received, and the market value of outstanding bonds in the series was 62.5 b.kr. at the end of 2020.

In order to smooth out the Treasury's redemption profile, switch auctions were held during the year, in which the Treasury bought back RIKS 21 0414 versus the sale of RIKB 22 1026 and RIKS 26 0216 in the amount of 7.7 b.kr. market value.

Concurrent with news reports about COVID-19, significant buying pressure developed on indexed Treasury bonds, partly because of strikes domestically and turmoil in foreign markets following the onset of the pandemic. This had a temporary negative impact on the domestic equity market, prompting investors to buy domestic Treasury bonds instead. Towards the end of Q1/2020, the Treasury announced a 40 b.kr. bond issue in Q2 in order to finance the expected deficit.

Chart V-5
Brakedown of Government debt
Year end 2020



Source: Central Bank of Iceland.

Chart V-6
Nominal Treasury bonds shorter than 5 years



Source: Central Bank of Iceland.

Chart V-7
Nominal Treasury bonds longer than 5 years



Source: Central Bank of Iceland.

The announcement caused yields to spike at the long end of the Treasury yield curve.

In Q3, the Treasury announced plans to issue bonds for up to 60 b.kr. to address the economic repercussions of the pandemic. As Q3 progressed, it grew clear that the Treasury's financing need would be greater than previously estimated, and towards the end of the quarter the Treasury announced that it would issue bonds for up to 70 b.kr. in Q4. Nominal yields began to rise as a result, as it had become clear that the supply of Treasury bonds would be larger than previously thought.

Treasury yields continued to rise in Q4, mainly because supply increased and one of the largest foreign bond holders closed out their position. At the end of the year Treasury domestic debt amounted to 979 b.kr., thereof 290 b.kr. indexed.

Foreign debt management

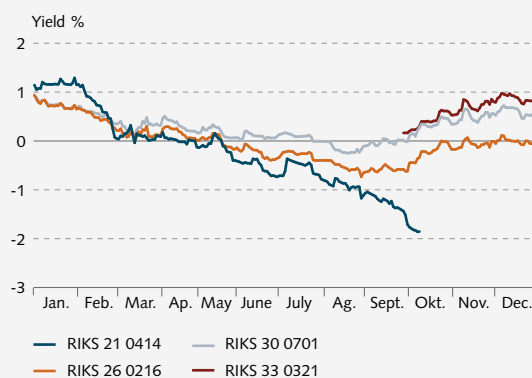
According to the *Medium-Term Debt Management Strategy* for 2020-2024, new Treasury loans taken in foreign currencies are used mainly to expand the Central Bank's international reserves, to refinance outstanding market issues, and to maintain access to foreign credit markets.

In 2020, the Treasury issued a foreign-denominated bond in the amount of 500 million euros. The bonds bear 0.625% fixed interest and were issued for six years at a yield of 0.667%. A marketable Treasury eurobond issued in 2014 matured in July. The original issue was for 750 million euros, but due to buybacks in 2017, the outstanding balance at maturity was only 292 million euros. At the end of the year, Treasury foreign debt totalled just under 246 b.kr.

State guarantees

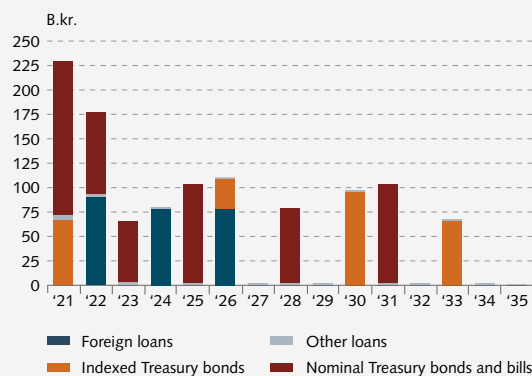
The Central Bank of Iceland handles tasks relating to Treasury guarantees and the State Guarantee Fund. The State Guarantee Fund oversees State guarantees and is tasked with keeping abreast of the activities of entities that have received State guarantees and maintaining a record of the obligations bearing such guarantees. The majority of State guarantees derive from the Government's holding in the Housing and Construction Authority. Parties that enjoy Government guarantees due to Government ownership are required to obtain the Central Bank's approval of the terms and conditions for loans they intend to take abroad. Treasury guarantees totalled 897 b.kr. at the end of 2020, as opposed to 920 b.kr. at year-end 2019.

Chart V-8
Inflation linked Treasury Bonds



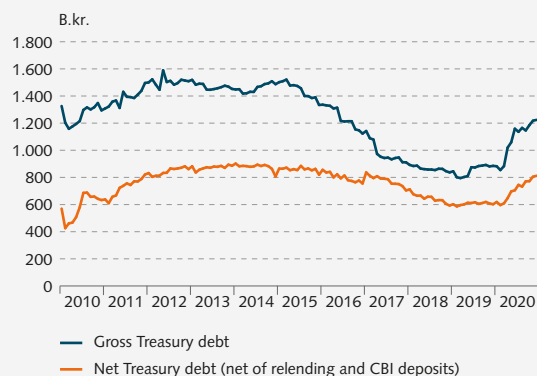
Source: Central Bank of Iceland.

Chart V-9
Redemption profile of government debt

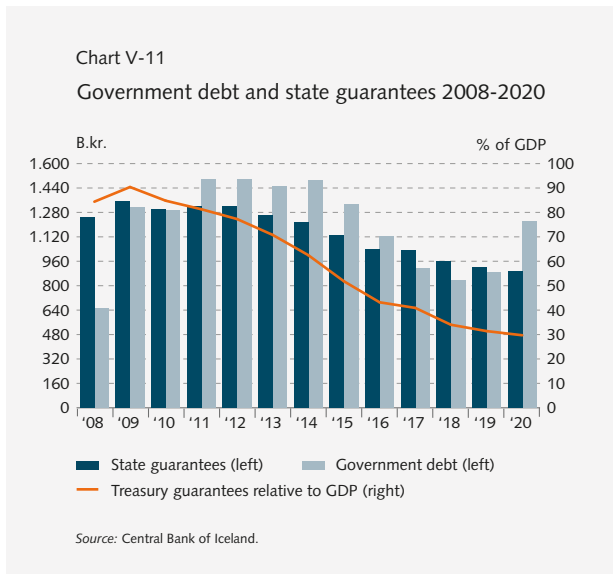


Source: Central Bank of Iceland.

Chart V-10
Treasury debt development



Source: Central Bank of Iceland.



Sovereign credit rating of the Republic of Iceland

Iceland's sovereign credit ratings affect the borrowing terms offered to it in foreign credit markets, as well as providing a benchmark for terms offered to other domestic borrowers. The Republic of Iceland receives regular credit ratings from three international agencies: Fitch Ratings, Moody's Investors Service, and S&P Global Ratings. As of end-2020, all three agencies' ratings for Iceland's long-term obligations in foreign and local currency were in the middle of the A category.

In May, Fitch affirmed Iceland's A rating for long-term obligations but changed the outlook to negative. The change in the outlook reflected weaker GDP growth, the impact of the pandemic on public finances, and the risk that the economic impact of the pandemic would be greater than previously forecast. In October, Fitch affirmed the sovereign rating and negative outlook.

In April, Moody's affirmed Iceland's sovereign rating of A2, with a stable outlook, noting that Iceland's strong asset position, robust institutions, and resilient economy would support the sovereign rating through the significant but temporary impact of COVID-19 on the country's economy and public finances. Moody's re-affirmed the A2 rating and stable outlook in October.

In May, S&P affirmed Iceland's sovereign ratings at A/A-1, with a stable outlook. In the rationale for the rating decision, the agency noted that the stable outlook reflected Iceland's strong fiscal and external positions, which afforded the Government the flexibility to respond to COVID-19 and the risks associated with it. S&P affirmed Iceland's sovereign rating again in October.

International co-operation

The Central Bank of Iceland communicates and conducts transactions with international institutions in its field. In view of the circumstances brought on by the COVID-19 pandemic, meetings with all of the Bank's partner institutions were held remotely during the year.

International Monetary Fund

The Central Bank formally represents Iceland at the International Monetary Fund (IMF). A mission from the IMF held discussions with the Icelandic authorities during the year, focusing on economic developments and prospects and the response to the pandemic. Because of COVID-19, the Fund did not publish its annual report on Iceland, but it consulted informally with member countries and provided special support to countries that had been hit hard by the pandemic.

Iceland collaborates with the Nordic and Baltic countries at the IMF and forms a Constituency with them. These countries together elect one permanent representative to the Executive Board, which comprises 24 members. The Constituency's representative on the Executive Board in 2020 was Mika Pösö from Finland. Each year, the Nordic-Baltic office compiles a report on the salient issues on the agenda of the Fund and the Executive Board during the year, including the Constituency's views on them. These reports are published on the Central Bank website.

The Fund's International Monetary and Financial Committee (IMFC), which generally holds two meetings a year, met twice in 2020. The Governor of the Central Bank is Iceland's representative on the IMF Board of Governors, which convenes each year at the Fund's annual meetings. The meetings in 2020 were held remotely.

Bank for International Settlements

The Central Bank is a shareholder in the Bank for International Settlements (BIS) in Basel, Switzerland. During the year, the Governor participated in both the BIS annual meeting and the regular governors' meetings, which are held every other month. All of the meetings were held remotely.

Organisation for Economic Co-operation and Development (OECD)

Central Bank representatives participate in the work of the Organisation for Economic Co-operation and Development (OECD). OECD experts also come to Iceland on a regular basis to keep abreast of economic

developments, and they issue periodic reports setting forth the Organisation's opinion of economic developments and prospects in the country.

Network for Greening the Financial System

In 2020, the Central Bank of Iceland became a member of the Network for Greening the Financial System (NGFS). The NGFS is a worldwide network of central banks and financial supervisors that have declared their willingness and commitment to working together to promote and develop best practices for managing climate- and environment-related risk in the financial sector and to promote sustainable and environment-friendly investment.

Collaboration in connection with financial supervision

The Central Bank of Iceland participates in the work of European financial supervisory bodies, including the European Banking Authority (EBA), the European Insurance and Occupational Pensions Authority (EIOPA), and the European Securities and Markets Authority (ESMA). In these fora, the Bank has the same rights and responsibilities as the supervisory authorities in EU member countries but does not have voting rights. Participation in the Board of Supervisors, permanent committees, and work groups of European supervisory bodies enables the Bank to keep abreast of legislative amendments and participate in developing European financial market legislation. With its participation, the Central Bank also does its part to ensure harmonised implementation of European financial market legislation in the EEA. Participation also underpins the implementation of new European legislation in Iceland, facilitates it, and contributes to more effective supervision after implementation is complete.

The Bank participated actively in international cooperation on measures to combat money laundering and terrorist financing, including through EBA committees and collaboration with the Nordic and Baltic countries.

The Central Bank also collaborates with other Nordic supervisory bodies in a task force entrusted with harmonising supervision of the Nasdaq securities exchanges in the Nordic region. The task force's chief role, in addition to conducting proactive investigations, is to assess and monitor key risks in the exchanges' operations.

Cooperation in connection with financial stability

The Central Bank participates in the work of the European Systemic Risk Board (ESRB) and thus has access to European analyses of systemic risk. The Governor attends meetings of the ESRB as an auditing member.

Furthermore, the Central Bank participates in the work of the Financial Stability Board (FSB), a cooperative forum for global financial stability.

The Bank also takes an active part in Nordic-Baltic cooperation, including through the Nordic-Baltic Macroprudential Forum, where the countries in the region exchange information on developments in systemic risk and the application of macroprudential tools. Moreover, the Bank participates with the Ministry of Finance and Economic Affairs in the activities of the Nordic-Baltic Cross-Border Stability Group, whose role is to coordinate responses to financial shocks affecting more than one country and to share information on financial stability among the institutions in the Nordic-Baltic region.

As in previous years, the Bank participated actively in international cooperation on developments in payment intermediation, including on digital cash and cybersecurity. The Bank also collaborated with other Nordic central banks on the establishment of an innovation centre on behalf of the Bank for International Settlements in Stockholm, as a contribution to analysis of innovation in the field of financial technology (fintech).

Currency swap agreement with the People's Bank of China

The People's Bank of China (PBC) and the Central Bank of Iceland concluded a new currency swap agreement during the year. The agreement was made for the first time in 2010 and then renewed in 2013 and 2016. The purpose is to promote trade between the two countries and support direct investment, as well as safeguarding financial stability. The new agreement is in the amount of 70 billion Icelandic krónur, or 3.5 billion Chinese yuan. It remains in effect for five years and is renewable at the end of that period.

Cash

At the end of 2020, cash issued by the Central Bank of Iceland amounted to 81.5 b.kr., including 77.1 b.kr. in banknotes and 4.4 b.kr. in coin. Cash issued by the Central Bank is recorded on the liabilities side of the Bank's balance sheet. Table 3 on page 88 shows the breakdown by banknote and coin denomination.

Discussions of cash in circulation usually refer to cash outside deposit institutions and central banks. The difference between this figure and the total in Table 3 on page 88, called the overnight cash balance, consists of cash on the assets side of deposit institutions' bal-

Jóhannes Nordal cultural heritage grants

The cultural heritage grant in the name of former Central Bank Governor Jóhannes Nordal was awarded for the ninth time on 25 June 2020. A total of 29 applications were received, and grants were awarded to three projects.

Fraedafélag um forystufé, the association for bellwether studies, at Svalbard in Thistilfjörður was awarded a 1.5 m.kr. grant to register all bellwether sheep in the country in a centralised database, *fjarvis.is*. This is the first step in a longer process, as it has been requested that bellwether sheep be listed by UNESCO as an animal species threatened with extinction.

Krumma films ehf. received a 1.5 m.kr. grant for the preservation of video resources documenting the battle for gay and lesbian rights in Iceland. The materials resulting from the production of the series *Svona fólk (Those People)* will be posted on the website *svonafolk.is*.

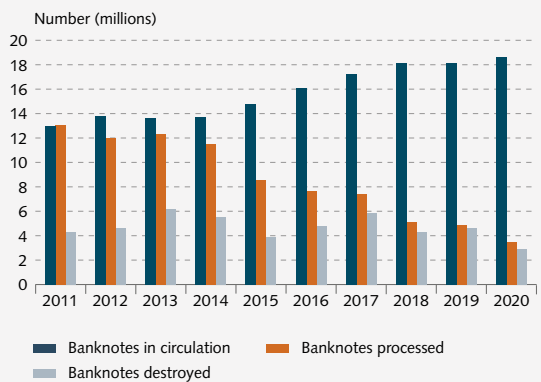
Sölvi Björn Sigurdsson received a grant of 1 m.kr. to create a book about the life of his grandfather, Magnús Ásgeirsson, a respected and prolific translator active in the first half of the 20th century. The book will also cover Magnús' interactions with well-known individuals whom he met.

Chart V-12
Cash in circulation



Source: Central Bank of Iceland.

Chart V-13
Banknotes processed, destroyed, and in circulation at each year-end



Source: Central Bank of Iceland.

ance sheets at the close of business. At the end of 2020, deposit institutions' overnight cash balance was 7.8 b.kr. Cash in circulation outside deposit institutions and the Central Bank (i.e., held by companies, individuals, etc.) totalled 73.7 b.kr. at the end of 2020, an increase of 7.0 b.kr., or 10.4%, between years. There are signs that use of cash in business transactions declined in 2020 and that use of cash as a store of value increased. One indication of this is that there were far fewer banknotes destroyed in 2020 than in 2019. Another is the increase in the number of 10,000 kr. banknotes in circulation.

At the end of 2020, there were 18.6 million banknotes in circulation in Iceland. For a relatively long period, the Central Bank has destroyed an average of roughly 5 million unfit banknotes per year. In 2020, the Bank destroyed 2.9 million notes that were considered unfit for use. The decline in the number of destroyed notes can be attributed to the COVID-19 pandemic.



Supervisory Board 2020, together with the Governor and the Board Secretary. From left: Bolli Hédinsson, Sigurdur Kári Kristjánsson; Una María Óskarsdóttir; Jacqueline Clare Mallett; Ásgeir Jónsson, Governor; Guðrún Sóley Gunnarsdóttir, Board Secretary; Thórunn Guðmundsdóttir, vice-chair; Frosti Sigurjónsson; and Gylfi Magnússon, chair.

Management, organisation, and human resources



Governors

During the year, Ásgeir Jónsson served as Governor of the Central Bank. He was appointed for a term of five years beginning on 20 August 2019. The Governor directs and is responsible for the Bank's activities and operations and is authorised to take decisions on all matters not entrusted to others by law.

In 2020, Rannveig Sigurdardóttir was Deputy Governor for Monetary Policy, Unnur Gunnarsdóttir was Deputy Governor for Financial Supervision, and Gunnar Jakobsson was Deputy Governor for Financial Stability. The Deputy Governors oversee the Bank's affairs in the areas they are appointed to lead, under the direction of the Governor.

Decisions on international reserve management and granting guarantees or loans to credit institutions experiencing liquidity problems are taken by the Governor and Deputy Governors in a meeting called by the Governor, as is provided for in Article 3, Paragraph 3 of the Act on the Central Bank of Iceland, no. 92/2019. Decisions on setting rules on special reserve requirements for new foreign currency inflows on the basis of the Foreign Exchange Act, decisions on setting rules on the operation of regulated foreign exchange markets, and decisions on organisation and the setting of rules on the Bank's activities shall be taken in the same manner.

Supervisory Board

The Supervisory Board monitors the Bank's compliance with the statutory provisions applying to its activities. In other respects, the Board undertakes such tasks as are outlined in Article 8 of the Central Bank Act.

At the beginning of 2020, the Bank's Supervisory Board was chaired by Gylfi Magnússon. Other members were Thórunn Gudmundsdóttir (vice-chair), Bolli Hédinsson, Una María Óskarsdóttir, Sigurdur Kári Kristjánsson, Jacqueline Clare Mallett, and Frosti Sigurjónsson. Thórlindur Kjartansson, Jóhanna Vigdís Gudmundsdóttir, Hildur Traustadóttir, Vilborg Sveinsdóttir, Kristín Thoroddsen, Ólafur Margeirsson, and Bára Ármannsdóttir served as alternates. The Board must be elected after each Parliamentary election. The last election took place in autumn 2017, and the Supervisory Board was elected on 18 April 2018. The Supervisory Board held 14 meetings over the course of 2020.

Organisational structure

At the beginning of the year, the Bank adopted a new organisational chart following the entry into force of the new Central Bank Act. According to Article 3, Paragraph 3 of the Act, the Governor and Deputy Governors decide the Bank's organisational structure, which the Supervisory Board then confirms; cf. Article 8, Item (a) of the Act. Under the new organisational chart, the Bank has seven core departments: Economics and Monetary Policy; Treasury and Market Operations; Financial Stability; Banking; Pensions and Insurance; Markets and Business Conduct; and Compliance and Inspections. There are four support departments: Operations, Information Technology and Statistics, Finance, and Human Resources. The organisational chart also includes the centralised General Secretariat. Each department is overseen by a departmental director. Four of the Bank's core departments have their origins in the

Financial Supervisory Authority, and three are from the Central Bank. Support departments from the two institutions were merged. This applies as well to the General Secretariat, where legal services, information activities, and services to the Governors merged.

The Supervisory Board oversees internal audit for the Bank and engages the Internal Auditor, as is provided for in Article 8, Item (d) of the Central Bank Act.

Departmental tasks

The General Secretariat oversees the affairs and activities of the Bank and assists in formulating and enforcing its policies, in cooperation with other departments. It provides advice and services to the Governor, Deputy Governors, Supervisory Board, committees, and departments of the Bank. The department's tasks include legal services; preparation of rules; regulatory compliance; communications with ministries, Parliament, and other domestic institutions; processing and follow-up of communications and queries received by the Bank; oversight of presentations and information disclosure by the Bank; and editorial and oversight of the Bank's Annual Report, website, and social media. In addition, the General Secretariat monitors the Bank's own risk, and a new Chief Risk Officer position was established during the year. The department also handles international cooperation, including with the International Monetary Fund.

The Economics and Monetary Policy Department carries out economic and monetary research, prepares macroeconomic and inflation forecasts, participates in formulating policy in currency and monetary matters, and analyses developments in domestic and foreign economic and monetary affairs, including the macroeconomic elements of financial stability. The Department oversees the issuance of various Bank publications, including *Hagvísar/Economic Indicators*, *Peningamál/Monetary Bulletin*, *Working Papers*, *Economic Affairs*, and *Economy of Iceland*. The department also oversees a range of projects relating to the work of the Bank's Monetary Policy Committee.

The Markets Department oversees the domestic money market and currency market, as well as transactions with domestic financial institutions. It also manages the Bank's balance sheet, handles the custody and investment of the international reserves, and manages Treasury debt, Treasury guarantees, and Treasury re-lending. The Department also oversees communications with the foreign financial institutions with which the Central Bank and the Treasury conduct business. It handles securities administration, payments for securities trans-

actions, and payments in connection with borrowing and swap agreements. Furthermore, it administers the Bank's interbank payment system and SWIFT system, as well as overseeing domestic and cross-border payments for the Bank, the Treasury, and State enterprises.

The Financial Stability Department analyses financial system risks, monitors credit institutions' liquidity and foreign exchange balance, and participates in formulating prudential rules for the financial system. The department also oversees the Foreign Exchange Act, the Act on the Treatment of Króna-Denominated Assets Subject to Special Restrictions, and rules issued on the basis of these Acts. In addition, it monitors the position of credit institutions, households, and businesses; payment flows to and from Iceland; and the external position of the economy. Moreover, the department monitors systemically important financial market infrastructure. The Bank's Resolution Authority, established in November 2020, is part of the Financial Stability Department. The department publishes the Bank's *Financial Stability* reports and oversees a variety of projects relating to the work of the Bank's Financial Stability Committee.

The Banking Department monitors the activities of commercial banks, savings banks, credit institutions, investment firms, and payment institutions. The department's primary tasks centre on the supervisory review and evaluation process. This includes assessments of capital and liquidity requirements; reviews of recovery plans; analysis and assessment of risks in supervised entities' operations; and communications with boards of directors, senior management, and external auditors. The Banking Department works with the Financial Stability Department on systemic risk assessments.

The Pensions and Insurance Department monitors the activities of insurance companies, pension funds, and private pension savings custodians. This entails, on the one hand, regular monitoring of insurance companies in accordance with FSA Iceland's risk-based supervision model, which defines the frequency with which key risk factors in the companies' operations are examined; and on the other hand, proactive checks carried out based on the circumstances in each given instance. The department analyses key risks and developments in the markets and monitors closely to ensure that the entities concerned satisfy the requirements for their operating licences, that their operating practices are in compliance with regulatory provisions, and that appropriate measures are taken at all times. It reviews insurers' own risk and solvency assessments (ORSA) and pension funds'

own risk assessments, for example, and interviews key employees.

The Markets and Business Conduct Department supervises entities in the securities market, including issuers of financial instruments, securities exchanges, central securities depositories, fund management companies, and alternative investment funds. The department also monitors transactions and conduct in the securities market (market manipulation and insider dealing). One of the tools it uses for this is an automated monitoring system that analyses transactions based on data submitted by financial institutions. Markets and Business Conduct also oversees consumer affairs, investor protection, and the business conduct of supervised entities. Monitoring of business conduct and investor protection entails, among other things, ensuring that supervised entities' customers are sold appropriate products and services, that information provided to them is neither misleading nor deceptive, and that action is taken in response to potential conflicts of interests.

The Compliance and Inspections Department works across other Bank departments involved in financial supervision. It conducts suitability assessments of supervised entities' managing directors and board members, grants and revokes operating licences, and processes notifications of qualifying holdings and applications for approval of mergers. The department also carries out on-site inspections with the aim of thoroughly analysing risks in supervised entities' activities and evaluating their internal controls, business plans or governance practices. Furthermore, it supervises obliged entities' measures to combat money laundering and terrorist financing.

The Operations Department carries out tasks involving the Bank's internal operations and the service it provides. Among these tasks are operation and administration of the Bank's real estate; oversight of and responsibility for specified security matters; purchasing for all Bank departments; expenditure control, including budget preparation; cafeteria and catering; management of the Bank's records in compliance with the Act on Public Archives; and operation of the Bank's library and numismatic collection.

The Finance Department oversees the Bank's financial information and that of companies owned by the Bank, as well as handling accounting for the National Festival gift from Norway and the Greenland Fund, which are administered by the Bank. It enters, processes, and discloses information in accordance with standard accounting and financial reporting practices and handles payroll processing for the Bank. In addition, it administers the Bank's position vis-à-vis the International Monetary Fund.

The department also handles the issuance and administration of banknotes and coin and operates the Bank's vaults.

The Information Technology and Statistics Department oversees and is responsible for the development, architecture, and operation of the Bank's information systems. It also handles the gathering, entry, and processing of statistics collected by the Bank, both for its own activities and for official statistical reporting. The Bank systematically collects information on the domestic credit market, the balance of payments, and the external position of the economy. These data form the basis for the Bank's assessment of important aspects of monetary developments and the financial system, and for regular disclosure of statistical information on its website and in its publications. The Bank publishes statistical information on the Statistics pages of its website.

The Human Resources Department is responsible for supporting the Bank's human resources policy at all times. The department's objective is to ensure harmonised implementation of personnel policies and provide targeted advice to management and employees so as to build up a workplace characterised by trust, professionalism, knowledge, and progressiveness. The main tasks of Human Resources are to manage staff recruitment and hiring, termination of employment, staff training, job development, workplace analysis and other analytical work, feedback interviews, decisions on remuneration, employee health and well-being, and equal rights.

The Internal Audit Department operates under the oversight of the Supervisory Board and is accountable to the Board for its activities. Internal Audit provides impartial, objective confirmation and advice to the Bank and companies owned by it, and it uses systematic audit procedures to evaluate the efficacy of risk management and governance practices within the Bank.

Central Bank committees

The Monetary Policy Committee (MPC) takes decisions on the application of the Bank's monetary policy instruments. These decisions must be based on the Bank's price stability objective and a thorough assessment of economic and monetary developments and prospects. The Committee takes interest rate decisions in support of the Bank's monetary policy objectives. It also takes decisions on transactions with credit undertakings other than loans of last resort. Furthermore, the Committee takes decisions on minimum reserve requirements, foreign exchange market transactions, and securities transactions undertaken with the aim of achieving the Bank's price stability objectives.

In 2020, MPC members were Governor Ásgeir Jónsson, who chairs the Committee; Rannveig Sigurdardóttir, Deputy Governor for Monetary Policy and vice-chair; Gunnar Jakobsson, Deputy Governor for Financial Stability; Gylfi Zoëga, professor at the University of Iceland; and Katrín Ólafsdóttir, Associate Professor at Reykjavík University.

The Central Bank Financial Stability Committee (FSN) takes decisions on the application of the Bank's financial stability policy instruments. Decisions taken by the Financial Stability Committee must be based on the law and on a thorough assessment of the current situation and outlook for the financial system. The tasks of the FSN are: (a) to assess developments and prospects for the financial system, systemic risks, and financial stability; (b) to define and discuss the measures deemed necessary at any given time to affect the financial system so as to strengthen and preserve financial stability, and submit comments to the relevant authorities when warranted; (c) to approve Government directives and take decisions with which the Committee is entrusted by law; and (d) to determine which supervised entities, infrastructure elements, and markets shall be designated as systemically important and of such a nature that their activities could affect financial stability.

Members of the Financial Stability Committee in 2020 were Governor Ásgeir Jónsson, who chaired the Committee; Gunnar Jakobsson, Deputy Governor for Financial Stability and vice-chair; Rannveig Sigurdardóttir, Deputy Governor for Monetary Policy; Unnur Gunnarsdóttir, Deputy Governor for Financial Supervision; Axel Hall, Assistant Professor at Reykjavík University; Bryndís Ásbjarnardóttir, Economist at Statistics Iceland; and Gudmundur Kristján Tómasson, former Director of Financial Market Infrastructure at the Central Bank of Iceland. In addition, a representative from the Ministry of Finance and Economic Affairs attends Committee meetings, with the right to address the meeting and present proposals.

The Financial Supervision Committee (FMEN) takes decisions entrusted to the Financial Supervisory Authority by law or Governmental directives. The Committee is authorised to entrust the Deputy Governor for Financial Supervision with taking non-major decisions. A list of decisions that are considered major can be found in Articles 4 and 5 of the Committee's rules of procedure.

During the year, members of the FSN were Ásgeir Jónsson, Governor, Unnur Gunnarsdóttir, Deputy Governor for Financial Supervision; Gunnar Jakobsson, Deputy Governor for Financial Stability; Andri Fannar Bergthórsson, Assistant Professor at Reykjavík

University; Ásta Thórarinsdóttir, Economist; and Guðrún Thorleifsdóttir, Director General at the Ministry of Finance and Economic Affairs. When decisions specified in Article 15, Paragraph 2 of the Act on the Central Bank of Iceland are taken, Governor Ásgeir Jónsson takes a seat on the Committee as its chair. In other instances, Unnur acts as chair and Gunnar Jakobsson acts as vice-chair.

Human resources

At the end of 2020, the Central Bank employed 303 members of staff in 300.7 full-time position equivalents. The year-on-year increase in staffing is due to the merger of the Central Bank of Iceland and the Financial Supervisory Authority, which took effect on 1 January 2020. At the end of the year, the Bank employed 163 men and 141 women.

There were 13 departmental directors: seven men and six women. In addition, there were 26 deputy directors and unit heads: 12 women and 14 men. At the year-end, 91% of the Bank's staff were university-educated. At the end of the year, the Central Bank-owned company Greidsluveitan ehf. employed 10 members of staff: five men and five women. Seventeen new employees were hired during the year, and 29 left the Bank. There were 14 summer employees in 2020.

The equal pay analysis taken within the Bank that year showed that there was no unexplained wage gap between men and women at the time.

Table 1. Number of employees, by department (table next to Human Resources subchapter)

<i>Department</i>	<i>Number</i>
Banking	24
Governors	4
Finance	12
Financial Stability	30
Economics and Monetary Policy	24
Internal Audit	3
Compliance and Inspections	26
Pensions and Insurance	13
Human Resources	6
Markets and Business Conduct	16
Markets	37
Operations	37
General Secretariat	26
Information Technology and Statistics	45
Total	303

Merger of the Central Bank of Iceland and the Financial Supervisory Authority

The Financial Supervisory Authority and the Central Bank of Iceland merged at the beginning of 2020. A new organisational structure took effect at that time, and several operational elements were integrated, particularly in support departments. Work was done towards merging the Bank's operations into its headquarters at Kalkofnsvegur 1 in Reykjavík. Renovation and maintenance began, with the aim of opening up space to make it available for more effective use. Most of the Financial Supervisory Authority's activities were moved from its previous location at Katrínartún to temporary premises at Kalkofnsvegur 2, thus enabling more efficient use of the Bank's cafeteria and other facilities. By the year-end, maintenance and renovation work was nearing completion on one of the five floors of the Bank's premises, and work had begun on another.

The impact of COVID-19

From March onwards, the COVID-19 pandemic made a significant impact on the Central Bank's activities. When the pandemic began to spread in Iceland, most of the Bank's staff were required to work remotely, and the equipment necessary for teleworking was provided. In addition, most meetings were held remotely instead of in person. When the first wave of the pandemic subsided in May, employees gradually returned to the workplace, but remote work resumed in September, when the second wave began, and continued through the year-end. Visits to the Bank were prohibited for much of the year, and the exhibition hall on the first floor was closed for the most part. For work carried out on the premises, employees were divided into pods or "quaranteams", in accordance with the instructions of the public health authorities, and cafeteria, cleaning, and other services were adapted to the new criteria.

Central Bank of Iceland 31 December 2020

Governor

Ásgeir Jónsson

Deputy Governors

Gunnar Jakobsson

Rannveig Sigurdardóttir

Unnur Gunnarsdóttir

Supervisory Board

Principal members

Gylfi Magnússon, chair

Thórunn Gudmundsdóttir, vice-chair

Bolli Hédinsson

Una María Óskarsdóttir

Sigurdur Kári Kristjánsson

Jacqueline Clare Mallett

Frosti Sigurjónsson

Alternates

Thórlindur Kjartansson

Jóhanna Vigdís Gudmundsdóttir

Hildur Traustadóttir

Valgerdur Sveinsdóttir

Kristín Thoroddsen

Ólafur Margeirsson

Bára Valdís Ármansdóttir

Principal Officers

General Secretariat:

Rannveig Júníusdóttir, Director

Finance:

Erla Gudmundsdóttir, Director

Financial Stability:

Haukur C. Benediktsson, Director

Economics and Monetary Policy:

Thórarinn G. Pétursson, Chief Economist

Human Resources:

Íris Guðrún Ragnarsdóttir, Director

Markets:

Sturla Pálsson, Director

Operations:

Thóra Helgadóttir, Director

Information Technology and Statistics:

Logi Ragnarsson, Director

Compliance and Inspections:

Björk Sigurgísladóttir, Director

Pensions and Insurance:

Rúnar Gudmundsson, Director

Banking:

Finnur Sveinbjörnsson, Director

Markets and Business Conduct:

Páll Fridriksson, Director

Internal Auditor:

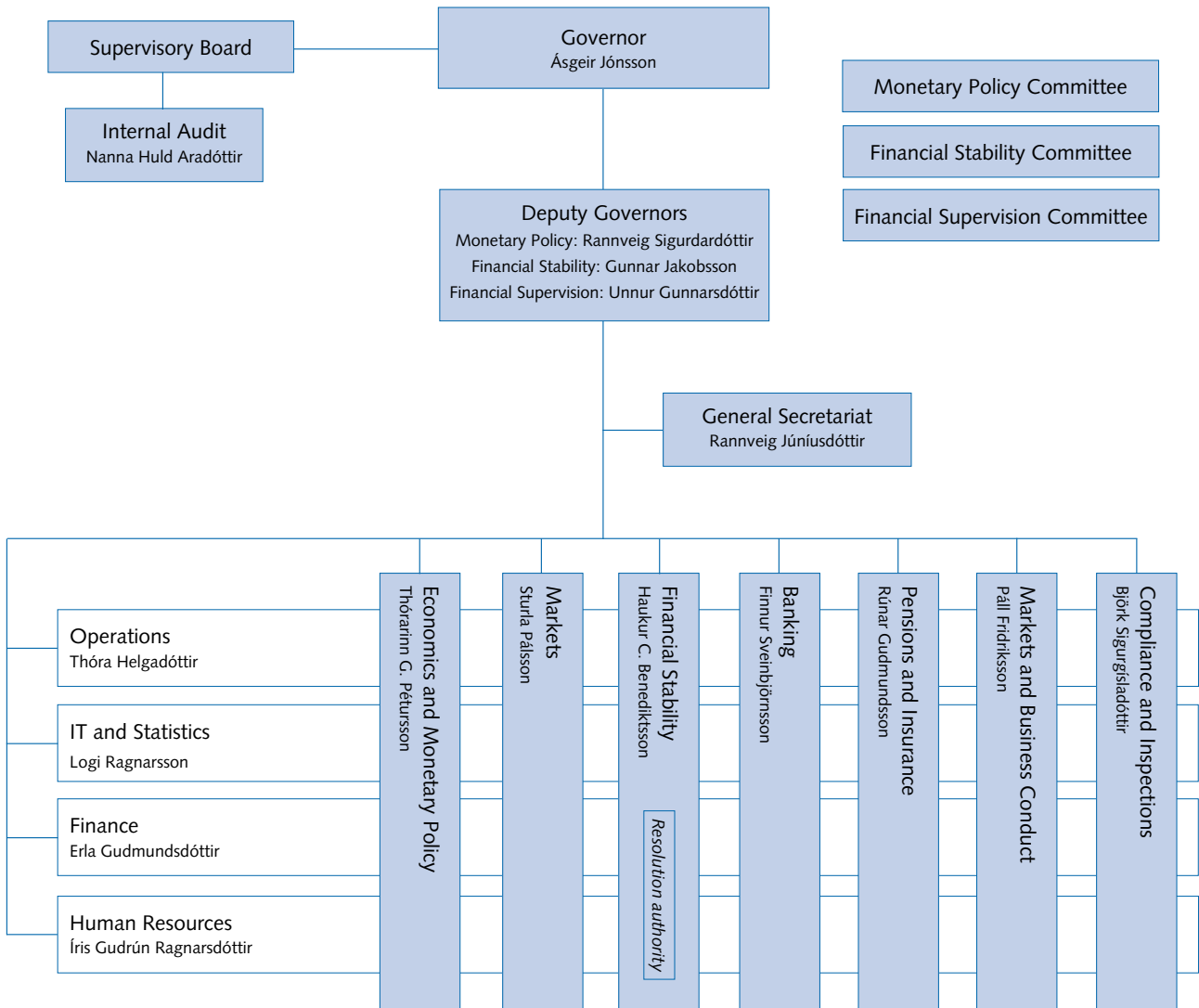
Nanna Huld Aradóttir

Company owned by the Central Bank of Iceland

Greidsluveitan ehf.:

Vigdís Ósk Helgadóttir, Director

Central Bank of Iceland — organisational chart



Operating results and balance sheet



The Bank recorded an operating profit of 68.3 b.kr. in 2020, as compared with a profit of 22.4 b.kr. in the previous year. Profits on the Bank's activities during the year are largely attributable to exchange rate differences and changes in asset values. The profit on financial instruments before exchange rate differences was 10.1 b.kr. in 2020, as compared with a loss of 2.5 b.kr. in 2019. The presentation of the Central Bank of Iceland's annual accounts has changed somewhat from the previous year in order to give a clearer view of the Bank's operations, balance sheet, and cash flow. The tables in the margin show the year-on-year changes in key items in the profit and loss account and balance sheet.

Net interest income totalled 74.5 m.kr. in 2020, as opposed to net interest expense of 9.2 b.kr. in the previous year. Interest income on domestic assets increased year-on-year by 24.4 m.kr., or 6.6%, whereas interest income on foreign assets declined by 2.2 b.kr., or 24.7%. Interest expense on domestic sight deposits and term deposits held with the Central Bank declined by 11.5 b.kr. between years. There were several reasons for this: the Bank lowered the policy rate during the year, it stopped offering one-month term deposits around mid-year, and it closed credit institutions' current accounts on 1 April, causing a reduction in deposits.

Exchange rate gains totalled 62.1 b.kr. in 2020, owing to the depreciation of the króna and the resulting rise in the value of the Bank's assets. Exchange rate gains were 28.5 b.kr. in 2019. The króna depreciated by 10.4% in trade-weighted terms from the beginning to the end of 2020. It depreciated by 14.9% against the euro, 5.1% against the US dollar, and 8.9% against the pound sterling.

Table 1 Profit and loss accounts highlights

<i>M.kr.</i>	2020	2019	<i>Change</i>
Net interest income (interest expense)	75	(9,190)	9,265
Changes in asset value	10,063	6,661	3,401
Revenues from shareholdings	0	46	(46)
Exchange rate difference	62,116	28,478	33,639
Gains on financial instruments	72,254	25,994	46,259
Operating revenues	3,354	1,009	2,345
Operating expenses	(7,413)	(4,748)	(2,665)
Effects of affiliated companies outside the group	55	209	(154)
Income tax	3	(20)	24
Outcome for the year	68,253	22,444	45,810

Tafla 2 Balance sheet highlights

<i>M.kr.</i>	2020	2019	<i>Change</i>
<i>Assets</i>			
Gold	15,404	11,720	3,684
Foreign-den. claims against non-residents	801,469	810,339	(8,870)
Foreign-den. claims against residents	0	38	(38)
Monetary policy-related claims against residents	9,520	0	9,520
Króna-den. claims against residents	5,809	5,935	(126)
Other assets	10,620	11,627	(1,007)
Assets, total	842,821	839,658	3,163
<i>Equity and liabilities</i>			
Equity	150,802	81,982	68,820
Issued banknotes and coin	81,462	74,734	6,728
Foreign-den. debt to non-residents	30,556	24,307	6,249
Foreign-denominated debt to residents	214,164	151,897	62,267
Króna-den. debt to non-residents	9,262	10,003	(741)
Monetary policy-related debt to domestic credit institutions	210,577	356,177	(145,599)
Króna-denominated debt to residents	144,926	139,899	5,027
Other liabilities	1,072	659	412
Equity and liabilities, total	842,821	839,658	3,163

Asset valuation adjustments were positive by 10.1 b.kr. in 2020, as compared with 6.7 b.kr. in 2019. The change is due to the significant decline in yields on foreign Treasury bonds held in the reserves during the year. Operating income increased by 2.2 b.kr. year-on-year, owing to income from financial supervision following the merger between the Bank and the Financial Supervisory Authority on 1 January 2020. Operating losses from supervision-related activities in 2020 totalled 58.8 m.kr. The Bank's operating expenses rose by 56% year-on-year because of costs associated with the merger with the Financial Supervisory Authority.

The Bank's assets totalled 842.8 b.kr. at year-end 2020, as opposed to 839.7 b.kr. at the end of 2019. Foreign assets increased by 5.2 b.kr. during the year. Even though foreign assets changed little, there was some intrayear volatility, in part because of the Bank's active intervention in the domestic foreign exchange market. The Bank bought euros in the domestic foreign exchange market for 11.7 b.kr. and sold euros in the amount of 143.4 b.kr. The Bank's capital totalled just over 150.8 b.kr. at the end of 2020, and the capital ratio was 17.9%, up from 9.8% at the end of 2019. Foreign assets accounted for 97% of the Bank's total assets at the end of 2020.

The Central Bank's accounts are presented later in this report.

Outlook and capital adequacy criteria

The Central Bank is required by law to have the financial strength needed to enable it to carry out its legally mandated role. In keeping with this, each year the Bank must determine capital adequacy criteria that reflect its need for capital and interest-bearing assets. The capital adequacy criteria are based on the Bank's operating expenses and the risks and uncertainties it faces at any given time. The decision on capital adequacy criteria is endorsed by the Supervisory Board. The capital benchmark was set at 150 b.kr. in 2020.

The Central Bank's operating performance has improved markedly in the recent term, and its capital has therefore increased. At the end of 2020, the Bank's capital totalled 150.8 b.kr., slightly above the benchmark endorsed by the Supervisory Board. At the end of 2019, it was 82 b.kr. The Bank did not call in capital from the Treasury in 2020, despite the statutory authorisation providing for callable capital ranging up to 57.2 b.kr. at the price level from the date the Act entered into force. The year-on-year increase in capital is attributable

mainly to the depreciation of the króna; the decline in the Central Bank's key interest rate, which led to a narrower interest rate spread; and improved returns on the international reserves.

The global economic situation remains highly uncertain because of the COVID-19 pandemic. To a large extent, economic developments will depend on how successful efforts to control the pandemic prove to be. As a result, there is still considerable uncertainty about the Bank's operations and need for capital in the long term.

A scenario analysis of possible developments in the Central Bank's operating performance and capital over the next three years generally indicates a weaker performance than in 2020, and therefore a reduction in capital. In view of this, it was not deemed necessary to change the capital adequacy benchmark set in 2020, and it was endorsed unchanged by the Supervisory Board at 150 b.kr.

Each year, a decision is taken on the disposition of the Bank's profit, in accordance with a method introduced with Act no. 122/2014. The Bank's profit, after allocations have been made to the reserve fund, is transferred to the Treasury, to the extent that it is not used to strengthen the Bank's capital. In accordance with Article 40, Paragraph 2 of the Act on the Central Bank of Iceland, the profit in excess of the amount used to satisfy the Bank's capital adequacy requirement for 2020 was transferred to the Treasury as a dividend in the amount of 802.1 m.kr.

Consolidated
Annual Accounts 2020



Table of Contents

Independent auditor's report	39
Confirmation by the management of the Central Bank of Iceland	41
Profit and Loss Account 2020	43
Balance Sheet 31 December 2020	44
Consolidated Statement of Changes in Equity	46
Consolidated Statement of Cash Flows	47
Notes	48
Presentation of profit and loss account and balance sheet	82
Presentation of profit and loss account 2019	82
Presentation of balance sheet 2019	82

Independent auditor's report

To the Supervisory Board and the Governor of the Central Bank of Iceland

Report on the Audit of the Consolidated Financial Statements

Opinion

We have audited the consolidated financial statements of the Central Bank of Iceland ("the Group") for the year 2020, which comprise the consolidated balance sheet as of 31 December 2020, the consolidated income statement, consolidated statement of cash flows, and consolidated changes in equity for the year then ended, and notes to the consolidated financial statements, including a summary of significant accounting policies and other explanatory information.

In our opinion, the accompanying consolidated financial statements give a true and fair view of the financial position of the Group as of 31 December 2020, and of its consolidated financial performance and its consolidated cash flows for the year then ended, in accordance with the Icelandic Annual Accounts Act.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (ISA). Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Consolidated Financial Statements* section of our report. We are independent of the Group in accordance with the ethical requirements that are relevant to our audit of consolidated financial statements in Iceland, and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Other information

The Supervisory Board and the Governor of the Central Bank are responsible for the other information. The other information comprises the Annual Report but does not include the consolidated financial statements and our auditor's report thereon. Our opinion on the consolidated financial statements does not cover the

other information, and we do not express any form of assurance conclusion thereon.

In connection with our audit of the consolidated financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the consolidated financial statements or the knowledge we obtained in our audit, or otherwise appears to be materially misstated. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. The Annual Report is not available on our reporting date but is expected to be made available to us after that date.

Responsibilities of the Supervisory Board and the Governor of the Central Bank for the Consolidated Financial Statements

The Supervisory Board and the Governor are responsible for the preparation and fair presentation of the consolidated financial statements in accordance with the Icelandic Annual Accounts Act, the Act on Financial Undertakings, and the Act on the Central Bank of Iceland, and for such internal control as they deem necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the consolidated financial statements, the Supervisory Board and the Governor are responsible for assessing the Group's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless they either intend to dissolve the Group or to cease operations, or have no realistic alternative but to do so.

The Supervisory Board and the Governor of the Central Bank are responsible for overseeing the Group's financial reporting process.

Auditor's Responsibilities for the Audit of the Consolidated Financial Statements

Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free of material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance but is not a guarantee that an audit conducted in accordance with the ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions taken by users on the basis of these consolidated financial statements.

As part of an audit in accordance with the ISAs, we exercise professional judgment and maintain professional scepticism throughout the audit. We also:

- Identify and assess the risk of material misstatement in the consolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Group's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of the management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether material uncertainty exists related to events or conditions that may cast significant doubt on the Group's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence up to the date of our auditor's report. However, future events or conditions may cause the Group to cease to continue as a going concern.
- Evaluate the overall presentation, structure, and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in manner that achieves fair presentation.
- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision, and performance of the group audit. We remain solely responsible for our audit opinion.

We communicate with the Supervisory Board regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

Reykjavík, 17 March 2021

KPMG ehf.

Hrafnhildur Helgadóttir

Confirmation by the management of the Central Bank of Iceland

The Supervisory Board and Governor of the Central Bank of Iceland hereby confirm the Bank's annual financial statements for the year 2020 with their signatures. Frosti Sigurjónsson expresses the reservation that he does not consider it appropriate to include banknotes and coin with liabilities in the balance sheet.

Reykjavík, 17 March 2021

Confirmation by the Supervisory Board

Gylfi Magnússon
chair

Thórunn Guðmundsdóttir
Sigurdur Kári Kristjánsson
Frosti Sigurjónsson

Bolli Hédinsson
Una María Óskarsdóttir
Jacqueline Clare Mallett

Confirmation by the Governor

Ásgeir Jónsson

Confirmation by the Prime Minister's Office

With reference to the statements by the auditors, the Supervisory Board, and the Governor, I hereby ratify these financial statements.

Reykjavík, 26 March 2021

Katrín Jakobsdóttir

Profit and Loss Account 2020

	Notes	2020	2019 ¹
Interest income from domestic assets	6	392,160	367,770
Interest income from foreign assets	6	6,852,230	9,098,747
Interest expense on domestic liabilities	7	(6,537,436)	(18,047,525)
Interest expense on foreign liabilities	7	(632,422)	(609,370)
Net interest income (expense)		<u>74,532</u>	<u>(9,190,378)</u>
Value adjustments of foreign assets		9,771,472	6,261,808
Value adjustments of domestic assets		291,187	399,588
Value adjustments, total	8	<u>10,062,659</u>	<u>6,661,396</u>
Revenues from shareholdings	9	0	45,550
Gains (losses) on financial instruments before exchange rate difference		10,137,191	(2,483,432)
Exchange rate difference	10	62,116,426	28,477,550
Gains on financial instruments		<u>72,253,617</u>	<u>25,994,118</u>
Revenues from supervision fees	11	2,359,005	0
Service revenues	12	903,831	962,757
Other revenues		91,451	46,621
Other revenues, total		<u>3,354,287</u>	<u>1,009,378</u>
Salaries and related expenses	13	(5,146,535)	(2,924,664)
Other operating expenses	14	(1,503,283)	(1,147,651)
Service expenses	15	(536,903)	(513,088)
Depreciation of property and equipment	22.1	(129,080)	(96,920)
Depreciation of software	22.2	(96,898)	(65,816)
Operating expenses, total		<u>(7,412,699)</u>	<u>(4,748,139)</u>
Effects of affiliated companies outside the group	22.3	55,016	208,606
Earnings before taxes		<u>68,250,221</u>	<u>22,463,963</u>
Income tax	16	3,226	(20,347)
Profit for the year		<u>68,253,447</u>	<u>22,443,616</u>

1. The presentation of the profit and loss account has been changed from the prior year, and comparison figures have been changed accordingly. Note 2 explains the changes made in the profit and loss account from the prior year.

Balance Sheet 31 December 2020

	Notes	2020	2019 ¹
Assets			
Gold	17	15,403,715	11,720,136
Claims on non-residents, foreign-denominated	18	801,469,348	810,339,269
Foreign bank deposits	18.1	109,886,615	210,157,700
Balance with IMF	18.2	33,696,074	30,744,446
Foreign securities and other reserve assets	18.3	657,805,606	569,308,426
Non-reserve assets	18.4	81,053	128,697
Claims on residents, foreign-denominated	19	0	37,536
Claims on residents, monetary policy-related	20	9,519,749	0
Treasury	20.1	7,770,361	0
Deposit institutions	20.2	1,749,388	0
Claims on residents, króna-denominated	21	5,808,631	5,934,698
Other assets	22	10,619,730	11,626,547
Fixed operational assets	22.1	7,928,990	7,789,802
Software	22.2	983,598	768,007
Other assets	22.3	1,707,142	3,068,738
Assets, total		<u>842,821,173</u>	<u>839,658,186</u>

1. The presentation of the balance sheet has been changed from the prior year, and comparison figures have been changed accordingly. Note 2 explains the changes made in the balance sheet from the prior year.

	Notes	2020	2019 ¹
<i>Equity and liabilities</i>			
<i>Equity</i>			
Capital		91,160,430	89,763,819
Uncalled capital		(59,659,430)	(58,262,819)
Value adjustment reserve		67,056,063	55,126,282
Revaluation of real estate and liquid assets		7,330,069	7,540,925
Unrealised share in profit of associates		26,896	251,966
Other equity (negative)		44,888,080	(12,438,271)
Total equity	23	150,802,108	81,981,902
<i>Liabilities</i>			
Banknotes and coin	24	81,462,111	74,734,419
Debt to non-residents, foreign-denominated	25	30,555,938	24,307,059
Deposits	25.1	9,927,305	5,464,064
Counterpart to IMF	18.2	20,628,633	18,842,995
Debt to residents, foreign-denominated	26	214,163,804	151,897,082
Debt to non-residents, króna-denominated	27	9,262,364	10,002,913
Deposits	27.1	2,494,998	2,486,891
Certificates of deposit	27.2	6,767,366	7,516,022
Debt to domestic credit institutions, monetary policy-related	28	210,577,243	356,176,697
Deposits	28.1	66,011,866	57,154,494
Minimum reserve requirements	28.2	24,487,312	20,849,825
Term deposits	28.3	112,948,802	245,475,217
Certificates of deposit	28.4	7,129,263	32,697,161
Debt to residents, króna-denominated	29	144,925,801	139,898,714
Treasury	29.1	142,289,342	81,640,230
Other entities	29.2	2,636,459	58,258,484
Other liabilities	30	1,071,804	659,400
Liabilities, total		692,019,065	757,676,284
Equity and liabilities, total		842,821,173	839,658,186

1. The presentation of the balance sheet has been changed from the prior year, and comparison figures have been changed accordingly. Note 2 explains the changes made in the balance sheet from the prior year.

Consolidated Statement of Changes in Equity

	<i>Capital</i>	<i>Uncalled capital</i>	<i>Value adjustment reserve</i>	<i>Real estate revaluation</i>	<i>Unrealised share in profit of associates</i>	<i>Other equity (negative)</i>	<i>Equity, total</i>
2020							
Equity 31 December 2019	89,763,819	(58,262,819)	55,126,282	7,540,925	251,966	(12,438,271)	81,981,902
Effect of new Central Bank Act	(1,062,819)	1,062,819					0
Effect of merger with Financial Supervisory Authority						690,870	690,870
Equity 1 January 2020	<u>88,701,000</u>	<u>(57,200,000)</u>	<u>55,126,282</u>	<u>7,540,925</u>	<u>251,966</u>	<u>(11,747,401)</u>	<u>82,672,772</u>
Indexation of uncalled capital	2,459,430	(2,459,430)					
Profit 2020			11,929,781		124,930	56,198,736	68,253,447
Dividend from subsidiaries					(350,000)	350,000	0
Real estate revaluation				(124,111)			(124,111)
Depreciation of revalued assets 2020				(86,745)		86,745	0
Equity 31 December 2020	<u>91,160,430</u>	<u>(59,659,430)</u>	<u>67,056,063</u>	<u>7,330,069</u>	<u>26,896</u>	<u>44,888,080</u>	<u>150,802,108</u>
2019							
Equity 1 January 2019	88,796,493	(57,295,493)	42,255,199	6,411,632	4,244,047	(26,077,233)	58,334,644
Indexation of uncalled capital	967,326	(967,326)					0
Dividend from subsidiaries					(4,282,055)	4,282,055	0
Profit 2019			12,871,084		289,975	9,282,558	22,443,617
Real estate revaluation				1,203,641			1,203,641
Depreciation of revalued assets 2019				(74,348)		74,348	0
Equity 31 December 2019	<u>89,763,819</u>	<u>(58,262,819)</u>	<u>55,126,282</u>	<u>7,540,925</u>	<u>251,966</u>	<u>(12,438,271)</u>	<u>81,981,902</u>

Note 5 discusses the merger between the Bank and the Financial Supervisory Authority. Note 23 discusses the accounting treatment of equity items, gives an itemisation of changes in the revaluation reserve during the year, and shows developments in the Bank's capital ratio in recent years.

Consolidated Statement of Cash Flows

	Notes	2020	2019
<i>Operating activities</i>			
Collected interest income		10,776,066	11,246,831
Paid interest expense		(6,458,100)	(18,914,962)
Collected interest (paid)		<u>4,317,966</u>	<u>(7,668,131)</u>
Collected supervisory revenues		2,359,005	0
Collected service revenues and other revenues		1,001,850	980,169
Paid service expense		(538,344)	(529,433)
Paid-in dividends on shareholdings	9	0	45,550
Paid operating expense		(6,518,721)	(4,010,678)
Paid taxes		(23,446)	(54,923)
Net cash from (to) operating activities		<u>598,310</u>	<u>(11,237,446)</u>
<i>Investment activities</i>			
Securities purchased in international reserves	18.3	(364,111,453)	(114,825,299)
Securities sold and collected in international reserves		340,426,089	150,384,547
Changes in foreign non-reserve assets		100,738	146,573
Treasury securities purchased	20.1	(7,566,030)	0
Collected króna-denominated instalments on securities		186,460	160,196
Other assets		(1,748,243)	(1,343,630)
Operational assets purchased	22.1	(341,406)	(26,029)
Software purchased	22.2	(310,349)	(241,099)
Net investment in subsidiaries outside the group	22.3	0	(757,789)
Dividends paid by companies outside the group	22.3	350,000	4,282,055
Claims against subsidiaries outside the group	33	1,390,798	0
Investment activities, total		<u>(31,623,396)</u>	<u>37,779,525</u>
<i>Financing activities</i>			
Issued banknotes and coin	24	6,727,692	1,961,281
Foreign-denominated deposits		39,851,539	34,917,961
Króna-denominated deposits		(114,699,545)	20,964,526
Certificates of deposit		(26,316,554)	4,113,588
Other liabilities		(196,371)	69,950
Financing activities, total		<u>(94,633,239)</u>	<u>62,027,306</u>
Foreign bank deposits, increase (decrease)		(125,658,325)	88,569,385
Exchange rate difference on foreign bank deposits	10	25,387,239	2,493,526
Foreign cash balance at beginning of year		210,157,700	119,094,789
Foreign cash balance at end of year	18	<u>109,886,615</u>	<u>210,157,700</u>

Notes

General 49

1 Information on the institution	49
2 Basis for accounting methods	49
3 Accounting estimates and decisions	51
4 The group	51
5 Merger of the Central Bank of Iceland and the Financial Supervisory Authority	52

Notes to the profit and loss account 53

6 Interest income	53
7 Interest expense	54
8 Changes in asset value	54
9 Revenues from shareholdings	55
10 Exchange rate difference	55
11 Supervisory revenues	56
12 Service revenues	56
13 Salaries and related expenses	57
14 Other operating expenses	57
15 Service expenses	57
16 Income tax	58

Notes to the balance sheet 58

17 Gold	58
18 Claims on non-residents, foreign-denominated	58
19 Claims on residents, foreign-denominated	60
20 Claims on residents, monetary policy-related	60
21 Claims on residents, króna-denominated	60
22 Other assets	61
23 Equity	64
24 Issued banknotes and coin	66

25 Debt to non-residents, foreign-denominated	66
26 Debt to residents, foreign-denominated	66
27 Debt to non-residents, króna-denominated	67
28 Debt to domestic credit institutions, monetary policy-related	67
29 Debt to residents, króna-denominated	68
30 Other liabilities	68

Other information 69

31 The króna system	69
32 Foreign exchange transactions during the year	69
33 Related parties	71
34 Cost analysis	72
35 Financial supervision	73
36 Other matters	73
37 Events after the financial reporting date	73

Risk management 73

38 International reserves	74
39 Claims risk	74
40 Liquidity risk	76
41 Settlement risk	77
42 Market risk	78
43 Risk relating to domestic market transactions and deposits	80

Important accounting principles 80

44 Important accounting principles	80
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General

Note 1 – Information on the institution

The Central Bank of Iceland is an independent institution owned by the State and operating under the auspices of the Prime Minister. Its objective is to promote price stability, financial stability, and sound and secure financial activities. The Bank shall also undertake such tasks as are consistent with its role as a central bank, such as maintaining international reserves and promoting a safe, effective financial system, including domestic and cross-border payment intermediation.

As of 1 January 2020, the Central Bank is responsible for the tasks entrusted by law and Governmental directives to the Financial Supervisory Authority, and the Financial Supervisory Authority is now part of the Central Bank. The Bank shall therefore monitor supervised entities to ensure that their activities are in compliance with the law and with Governmental directives, and that they are in other respects consistent with sound and appropriate business practices.

Note 2 – Basis for accounting methods

The Central Bank of Iceland's consolidated annual accounts for the year ended 31 December 2020 are prepared in accordance with the Act on the Central Bank of Iceland, no. 92/2019, and the Annual Accounts Act, no. 3/2006. The consolidated annual accounts are based on cost-price accounting methods, except for financial assets held for trading and real estate, which are entered at fair value. Financial asset held for trading include marketable bonds and derivatives. The consolidated annual accounts have been prepared using the same accounting methods as in the prior year. The consolidated annual accounts are prepared in Icelandic krónur. All amounts are presented in thousands of Icelandic krónur. Information on the accounting methods can be found in Note 44.

Changes in presentation of the consolidated annual accounts

It was decided to change the presentation of the Bank's annual accounts in order to give a clearer view of the Bank's operations, balance sheet, and cash flow.

The Bank's balance sheet and profit and loss account are not set up in accordance with the Regulation on Presentation and Contents of Annual Financial Statements and Consolidated Annual Financial Statements, no. 696/2019. Such a presentation would give an unclear view of the Bank's balance sheet and profit and loss account, as the Central Bank of Iceland's activities are very different from the activities of the companies to which the Regulation pertains, most of which are operated for profit.

Changes in presentation of the balance sheet

The presentation of the Central Bank's balance sheet in the prior year can be seen in the Appendix. The new presentation contains more detailed itemisation than before, as it shows subcomponents of those components that comprise more than one item.

Gold is still the uppermost item listed in the Bank's balance sheet. It is followed by the item *Claims on non-residents, foreign-denominated*, which contains the subcomponents *Foreign bank deposits*, *Balance with the IMF*, *Foreign securities and other reserve assets*, and *Non-reserve assets*. In the previous year, the item *Foreign assets* comprised all of these subcomponents, except that it comprised *Balance with the IMF* only in part. In the prior year, *Balance with the IMF* was labelled *FX balance with the IMF*, and a portion of the balance was included under *Foreign assets*.

Next is the item *Claims on residents, foreign-denominated*, which was previously included with *Other assets*. This is followed by the *Claims on residents, monetary policy-related*, which did not appear previously because the balance was zero.

Next is *Claims on non-residents, króna-denominated*, which was previously part of the item *Domestic financial assets*. The last item on the assets side of the balance sheet is *Other assets*, which includes the subcomponents *Fixed operational assets*, *Software*, and *Other assets*. In the consolidated balance sheet for 2019, *Fixed operational assets* and *Software* were entered to the same line, under *Fixed operational assets*. In view of the scope of *Software*, it is considered appropriate to enter it separately in the balance sheet; therefore, it is now presented as a separate balance sheet item.

No year-on-year changes were made to the presentation of equity in the balance sheet.

Issued banknotes and coin is still the uppermost liabilities item. This is followed by *Debt to non-residents, foreign-denominated*, which comprises *Deposits*, which were previously classified as part of *Other deposits*, and *Counterpart to IMF*, which is classified in the same way as in the prior year.

The next item is *Debt to residents, foreign-denominated*, which was previously included with *Other deposits*. It is followed by the *Debt to non-residents, króna-denominated*, which includes *Deposits and Certificates of deposit*. In the prior year, the deposits were included with *Other deposits*, and *Certificates of deposit* were included with *Foreign liabilities*.

The next item is *Debt to domestic credit institutions, monetary policy-related*. It comprises *Deposits and Reserve requirements*, which were previously classified as *Deposits of financial institutions*; and *Term deposits and Certificates of deposit*, which were previously included with *Domestic financial liabilities*.

The next item is *Debt to residents, króna-denominated*. This item includes the subcomponents *Treasury and Government institutions* and *Other entities*, which were classified as *Other deposits* in the prior year; furthermore, debt to the Treasury, which was previously included under *Other liabilities*, was moved and is included under *Treasury and Government institutions*. The final item is *Other liabilities*, which was previously classified as *Other liabilities and Pension obligations*.

Changes in presentation of the profit and loss account

The presentation of the Central Bank's profit and loss account in the prior year can be seen in the Appendix.

It was decided to present *Gains (losses) on financial instruments* at the top of the profit and loss account, as it is the item that has the greatest impact on the Bank's operating performance. *Interest income* and *Interest expense* are still the uppermost items in the profit and loss account. In this year's profit and loss account, this is followed by *Value adjustments*, which were previously included with *Operating revenues*. After this is *Revenues from shareholdings*, previously included with *Operating revenues*. This is followed by a new subtotal: *Gains (losses) on financial instruments before exchange rate difference*. Below this is *Exchange rate difference*, which was previously the bottom item in the profit and loss account. Furthermore, this item now includes a component previously called *Exchange rate gains (losses) on foreign exchange transactions*, which was included with *Operating revenues*. This is followed by a new subtotal: *Gains (losses) on financial instruments*.

The next section is *Other revenues*. This includes *Service revenues*, previously listed in the *Operating revenues* section.

Other revenues is followed by *Operating expenses*. The first item in the *Operating expenses* section is *Salaries and related expenses*, followed by *Other operating expenses*. This is

unchanged from the prior year. This year, the item *Other operating expenses* includes *Impairment of claims and Expense due to banknotes and coin*, which were previously listed separately in the profit and loss account. *Other operating expenses* is followed by *Service expenses*, which previously appeared in the section *Operating revenues*. The final item under *Operating expenses* is *Depreciation of property and equipment*.

Effects of affiliated companies is a separate item following *Operating expenses*. This presentation is unchanged from the prior year. This is followed by the subtotal *(Loss) profit before taxes*, which was previously entitled *Operating loss before tax and exchange rate difference*. The next item, *Income tax*, is unchanged from the prior year. Last year, this was followed by *Loss without exchange rate difference*, which is not included in the current presentation.

Changes in presentation of the statement of cash flows

The presentation of the statement of cash flows was changed to reflect the changes in presentation of the Bank's balance sheet. In the opinion of management, the updated classification gives a clearer view of the Bank's cash flows.

Changes in the presentation of notes to the financial statements

The presentation of the notes to the financial statements was updated concurrent with the changes to the presentation of the profit and loss account and balance sheet. Furthermore, information on accounting principles is now found at the end of the notes, whereas it previously appeared at the beginning of the notes.

Comparison figures

In the 2019 financial statements, *Other operating expenses* were itemised in the notes, as follows: *Outsourced services*, *Operation of assets and liquid assets*, and *Sundry operational items*. At the beginning of 2020, the itemisation of *Other operating expenses* was updated in the group accounts and is now presented as follows: *Operation of assets and liquid assets*, *Information technology*, *Outsourced services*, *Office expense*, and *Sundry operational items*. Comparison figures have been changed accordingly.

Note 3 – Accounting estimates and decisions

In preparing the annual accounts, management must take decisions, make estimates, and draw conclusions that affect the application of accounting principles, as well as affecting the presented amounts of assets and liabilities, and income and expenses. The final results may differ from these estimates.

Management reviews estimates and underlying assumptions and makes changes as is deemed necessary. Changes in accounting estimates are recognised in the period in which they take place.

Note 4 – The group

Subsidiaries are companies controlled by the group. Control exists if the group bears the risk, is entitled to enjoy the variable benefits of its participation in the company, and can, through its decision-making power, affect the returns on the investment. The accounts of Greidsluveitan are included in the consolidated accounts from the time control was established until that control ends. The accounts of real estate company F fasteigna-

félag ehf. are held outside the group because they do not have a material impact on the operations and balance sheet of the group. The holding in F fasteignafélag ehf. is entered using the equity method.

Positions and transactions and all unrealised revenues and expenses between companies in the group are omitted from the consolidated financial statements.

	<i>Ownership share</i>	<i>Activities</i>
<i>Companies within the group</i>		
Greidsluveitan ehf., Álþheimar 74, Reykjavík	100%	Payment system operations
<i>Company outside the group</i>		
F fasteignafélag ehf., Ránargata 18, Reykjavík	100%	Holding company

Note 5 – Merger of the Central Bank of Iceland and the Financial Supervisory Authority

With the Act on the Central Bank of Iceland, no. 92/2019, which entered into force on 1 January 2020, the Central Bank of Iceland and the Financial Supervisory Authority merged under the name of the former.

The Central Bank is required to prepare its accounts in accordance with the Annual Accounts Act. The Annual Accounts Act specifies that when companies merge, accounts shall be prepared for the combined assets and liabilities of the companies.

With the merger of the Central Bank of Iceland and the Financial Supervisory Authority, it is appropriate to use the pooling of interests method, as both institutions were owned by the same party (the State) and no purchase price was paid at the time of the merger.

According to the pooling of interests method, individual balance sheet items as of the merger date are summed at book value.

The Financial Supervisory Authority prepared its accounts in accordance with the Act on Public Finances, no. 123/2015. The book value of the Financial Supervisory Authority's assets and liabilities was adjusted so that it is estimated in accordance with the Annual Accounts Act and not the Act on Public Finances.

The difference in the book value of the Financial Supervisory Authority's assets and liabilities according to the Annual Accounts Act versus the Act on Public Finances is recognised as equity.

Comparison figures do not include figures from the Financial Supervisory Authority.

Impact on the Bank's profit and loss account

The impact of the merger on the Bank's profit and loss account shows mainly in Supervisory revenues, Salaries and related expenses, and Other operating expenses. Comparison figures do not include figures from the Financial Supervisory Authority; i.e., the unit that discontinues operations. Supervisory revenues amounted to 2,359 m.kr. in 2020 but were zero in 2019. The table below shows Salaries and related expenses and Other operating expenses for the Central Bank of Iceland group and the Financial Supervisory Authority in 2019, compared with expenses for the merged institution in 2020.

	2020		2019	
	Central bank of Iceland	Financial Supervisory Authority (FME)	Central bank of Iceland (CBI)	Total (CBI + FME)
Salaries and related expenses	5,146,535	1,830,458	2,924,664	4,755,122
Other operating expenses	1,503,283	406,045	1,147,651	1,553,696
Depreciation of property, equipment, and software	225,978	19,865	162,736	182,601

Impact on the Bank's balance sheet

The Financial Supervisory Authority's assets and liabilities have been entered to the merger account, estimated according to the Annual Accounts Act. The impact on the Bank's balance sheet is negligible.

Impact on the merger account

<i>Assets</i>	
Fixed operational assets	50,973
Software	2,140
Other assets	866,631
Assets, total	919,744
<i>Equity and liabilities</i>	
<i>Equity</i>	
Other equity	690,870
Total equity	690,870
<i>Liabilities</i>	
Other liabilities	228,874
Liabilities, total	228,874
Equity and liabilities, total	919,744

Notes to the profit and loss account

Note 6 – Interest income

	2020	2019
<i>Interest income from domestic assets</i>		
Interest income from overnight loans and credit lines	766	1,171
Interest income from collateralised loans	6,638	0
Interest income from non-indexed securities	23,276	0
Interest income from indexed securities	348,889	350,550
Interest income from other domestic assets	12,591	16,049
Interest income from domestic assets, total	<u>392,160</u>	<u>367,770</u>
<i>Interest income from foreign assets</i>		
Interest income from balance with IMF	64,237	297,945
Interest income from bank accounts	197,164	1,250,022
Interest income from securities	6,365,574	7,179,610
Interest income from other foreign assets	225,255	371,170
Interest income from foreign assets, total	<u>6,852,230</u>	<u>9,098,747</u>

Interest income from domestic assets rose by 24.4 b.kr. from the year 2019, or by 6.6%.

In 2020, a total of 16 overnight loans were granted in the amount of 3.6 b.kr., as compared with 20 overnight loans totalling 5.7 b.kr. in 2019. The Bank stopped offering conventional overnight loans when the new interbank payment system was launched in October. Instead, banks have access to credit lines within the interbank system. One such credit line was granted in the amount of 3.7 b.kr.

Interest income from collateralised loans in 2020 was due mainly to the special collateralised loans offered by the Bank to commercial banks and savings banks beginning in September, in connection with support loans bearing a 100% Treasury guarantee. One conventional collateralised loan in the amount of 5 b.kr. was granted in 2020. No collateralised loans were granted in 2019.

At the beginning of May 2020, the Bank began buying Treasury bonds in the secondary market. This explains the interest income from non-indexed bonds.

Interest income from domestic assets declined by 2.2 b.kr. from the year 2019, or by 24.7%.

Interest income from foreign bank accounts declined by 84.2%, or by 1.1 b.kr. This is because the US Federal Reserve stopped paying interest in mid-March. Interest expense on foreign bank accounts bearing negative interest rates is expensed. Total interest on foreign bank accounts, adjusted for accounts bearing negative interest rates, was negative in the amount of 354 m.kr., a reduction of 1.2 m.kr. relative to 2019.

Interest income from foreign securities fell by 814 m.kr., or 11.3%. This was due to a decline in foreign market yields.

Note 7 – Interest expense

	2020	2019
<i>Interest expense on domestic assets</i>		
Interest expense on certificates of deposit	0	93,848
Interest expense on term deposits	3,951,380	9,497,254
Interest expense on current accounts	2,272,057	7,766,283
Interest expense on FX-accounts	542	4,340
Interest expense on other domestic liabilities	313,457	685,800
Interest expense on domestic assets, total	<u>6,537,436</u>	<u>18,047,525</u>
<i>Interest expense on foreign assets</i>		
Interest expense on balance with IMF	41,149	189,283
Interest expense on foreign bank accounts	551,169	420,087
Interest expense on foreign securities in international reserves	40,104	0
Interest expense on foreign assets, total	<u>632,422</u>	<u>609,370</u>

Interest expense on domestic liabilities declined by 63.8% between years. This is due to a lower policy interest rate during the year.

Interest expense on term deposits totalled 4 b.kr. in 2020, as opposed to 9.5 b.kr. in 2019. The Bank stopped offering one-month term deposits at mid-year. Instead, it introduced a new type of term deposit that can be used as payment system collateral, but with various commitment periods. Seven-day term deposits are still available.

Interest expense on current accounts declined by 5.5 b.kr., or 70.7%, as a result of lower interest rates and reduced deposit balances during the year.

Interest expense on foreign assets increased because of lower foreign interest rates, which results in higher negative interest on assets. This is offset by lower interest expense on the balance with the International Monetary Fund (IMF).

Interest expense on foreign bank accounts increased by 131.1 m.kr., or 31.2%, owing to negative interest on deposit balances.

Note 8 – Changes in asset value

	2020	2019
<i>Realised revaluation</i>		
Domestic securities	(4,217)	0
Foreign securities and securities funds	3,186,360	156,215
Realised revaluation, total	<u>3,182,143</u>	<u>156,215</u>
<i>Unrealised revaluation</i>		
Domestic securities	86,956	93,987
Domestic derivatives	208,448	305,601
Foreign securities and securities funds	6,791,345	6,415,025
Foreign derivatives	(206,233)	(309,432)
Unrealised revaluation, total	<u>6,880,516</u>	<u>6,505,181</u>
Value adjustments, total	<u>10,062,659</u>	<u>6,661,396</u>

Note 9 – Revenues from shareholdings

Revenues from shareholdings in 2019 are due to dividends from the Bank for International Settlements (BIS). Because of the spread of the COVID-19 pandemic, the BIS decided not to pay dividends in 2020.

Note 10 – Exchange rate difference

	2020	2019
<i>Realised exchange rate difference</i>		
Foreign bank deposits	25,387,239	2,504,323
Foreign securities and funds	57,339,798	18,289,859
Domestic foreign-denominated bank deposits	(26,817,912)	847,505
Derivatives	(2,215)	(10,653)
Other	17,992	(7,664)
Realised exchange rate difference, total	<u>55,924,902</u>	<u>21,623,370</u>
<i>Unrealised exchange rate difference</i>		
Gold	3,683,579	2,206,933
International Monetary Fund	1,142,998	415,952
Foreign securities and funds	1,369,903	4,222,962
Derivatives	0	9,323
Other	(4,956)	(990)
Unrealised exchange rate difference, total	<u>6,191,524</u>	<u>6,854,180</u>
Exchange rate difference, total	<u>62,116,426</u>	<u>28,477,550</u>

	<i>Average exchange rate for the year</i>		<i>Year-end exchange rate</i>		<i>Change in year-end exchange</i>
	2020	2019	2020	2019	%
Euro (EUR)	154.52	137.30	156.10	135.83	14.92
US dollar (USD)	135.27	122.65	127.21	121.10	5.05
Pound sterling (GBP)	173.59	156.49	173.55	159.42	8.86
Japanese yen (JPY)	1.27	1.13	1.23	1.12	9.82
Danish krone (DKK)	20.73	18.39	20.98	18.18	15.40
Norwegian krone (NOK)	14.42	13.94	14.93	13.77	8.42
Swedish krona (SEK)	14.75	12.97	15.57	12.99	19.86
Swiss franc (CHF)	144.33	123.46	144.38	125.14	15.37
Canadian dollar (CAD)	100.95	92.46	99.91	92.94	7.50
Chinese yuan (CNY)	19.62	17.75	19.45	17.40	11.78
Special drawing rights (XDR)	188.52	169.44	183.85	167.75	9.60
Gold (XAU)	240.145.82	170.898.00	240.817.43	183.741.00	31.06

Total foreign-denominated assets and liabilities, in ISK thousands

	31.12.2020		31.12.2019	
	Assets	Liabilities	Assets	Liabilities
Euro	359,763,714	230,693,054	296,735,960	163,118,789
US dollar	317,398,872	8,495,056	372,611,624	8,081,099
Pound sterling	91,287,299	1,653,105	100,981,453	1,543,137
Yen	27,699,601	1,647,806	35,192,183	1,485,473
Other currencies	5,458,728	2,233,515	4,866,318	1,985,811
Gold	15,403,715	0	11,720,136	0
Total	<u>817,011,929</u>	<u>244,722,536</u>	<u>822,107,674</u>	<u>176,214,309</u>

A further itemisation of total foreign-denominated assets and liabilities can be found in Note 42. Special drawing rights (SDR) are a currency basket determined by the IMF. The basket comprises five currencies: US dollar, euro, Chinese yuan, pound sterling, and Japanese yen. The Bank's only asset denominated

in SDR is its balance with the IMF, and its only SDR-denominated liability is the counterpart to the IMF. The Bank's SDR-denominated assets and liabilities are converted to the currencies comprising the currency basket, using the weight of each at the year-end.

Note 11 – Supervisory revenues

2020

Supervised entities and other entities subject to fees as specified in the Act on the Payment of Costs for Official Supervision of Financial Activities, no. 99/1999, shall pay the cost of operating the Central Bank Financial Supervisory Authority (FSA Iceland) by means of a special supervision fee.

Regular supervision	2,330,500
Extra supervision	<u>28,505</u>
Supervisory revenues, total	<u>2,359,005</u>

If FSA Iceland considers supervision of specific supervised entities to be considerably more costly and labour-intensive than the estimate for regular supervision provides for, the Central Bank may decide that the supervised entity concerned shall be required to pay for the necessary extra supervision.

Note 12 – Service revenues

2020

2019

Payment intermediation	748,169	814,365
Market transactions	<u>155,662</u>	<u>148,392</u>
Service revenues, total	<u>903,831</u>	<u>962,757</u>

In 2020, the RÁS system and the netting and real-time gross settlement systems were closed down and their operation discontinued. The Bank's new interbank payment system replaced the netting and real-time gross settlement systems.

Note 13 – Salaries and related expenses

	2020	2019
Wages and salaries	4,188,471	2,354,438
Pension fund	588,247	350,328
Salary-related expenses	351,299	197,471
Contribution to pension obligations	18,518	22,427
Salaries and related expenses, total	<u>5,146,535</u>	<u>2,924,664</u>
Number of man-years	297	188

The number of man-years at the Financial Supervisory Authority in 2019 was 117.

Note 14 – Other operating expenses

	2020	2019
Operation of assets and liquid assets	415,070	256,268
Information technology	286,414	124,331
Outsourced services	296,398	338,307
Office expense	277,046	212,835
Sundry operational items	228,355	215,910
Operating expenses, total	<u>1,503,283</u>	<u>1,147,651</u>

Remuneration to auditors

	2020	2019
<i>Auditing of annual accounts</i>		
KPMG ehf.	8,444	9,465
Deloitte ehf.	0	3,380
<i>Consultancy and other services</i>		
Deloitte ehf.	4,166	5,515
PricewaterhouseCoopers ehf.	2,501	2,316
Remuneration to auditors, total	<u>15,111</u>	<u>20,676</u>

Note 15 – Service expenses

	2020	2019
Payment intermediation	402,895	448,149
Expense due to custodial fees	71,264	39,997
Portfolio investment	62,744	24,942
Service expenses, total	<u>536,903</u>	<u>513,088</u>

Note 16 – Income tax

The Central Bank of Iceland is exempt from income tax pursuant to Article 4 of the Income Tax Act, no. 90/2003. The income tax expensed in the consolidated annual accounts is due to Greidsluveitan ehf., a subsidiary of the Central Bank of Iceland.

Income tax is calculated and recognised in the accounts, and the amount capitalised in the profit and loss account is 3.2 m.kr. No income tax will be paid in 2021 because Greidsluveitan's income tax base is negative.

Notes to the balance sheet

Note 17 – Gold

	2020	2019
Balance at beginning of year	11,720,136	9,576,083
Recognised in fixed operational assets	0	(62,880)
Exchange rate difference	3,683,579	2,206,933
Balance at end of year	<u>15,403,715</u>	<u>11,720,136</u>
Gold holdings at the year-end, in ounces	63,797	63,797

In 2019, a gold bar was taken from the international reserves and given to the Bank's museum and numismatic collection.

Note 18 – Claims on non-residents, foreign-denominated

Note 18.1 – Foreign bank deposits

	31.12.2020	31.12.2019
Deposits with foreign central banks	108,970,004	164,057,203
Deposits with Bank for International Settlements	97	44,807,009
Balance with other foreign banks	916,514	1,293,488
Foreign bank deposits, total	<u>109,886,615</u>	<u>210,157,700</u>
Deposits available for withdrawal	104,492,911	143,100,466
Term deposits, available within three months	5,393,704	67,057,234
Foreign bank deposits, total	<u>109,886,615</u>	<u>210,157,700</u>

Note 18.2 – International Monetary Fund

Iceland's quota with the International Monetary Fund (IMF) totalled SDR 321.8 million at year-end 2020 (31.12.2019: SDR 321.8m). The Bank's end-2020 balance with the Fund totalled SDR 69.8m, which is the difference between the quota and the Fund's króna-denominated deposits with the Bank, adjusted for

the balance on the IMF's current account with the Bank. The SDR allocation totalled SDR 112.2 million at the end of 2020 (31.12.2019: SDR 112.3m).

	31.12.2020		31.12.2019	
	SDR	ISK	SDR	ISK
<i>Assets</i>				
Central Bank of Iceland quota	321,800	59,162,930	321,800	53,981,950
IMF deposit with Central Bank of Iceland	(252,002)	(46,330,568)	(252,002)	(42,273,336)
IMF current account with Central Bank of Iceland	6	1,103	6	1,007
Central Bank foreign currency balance with IMF	69,804	12,833,465	69,804	11,709,621
Central Bank foreign currency balance with IMF	69,804	12,833,465	69,804	11,709,621
Central Bank deposit balance with IMF	113,447	20,857,231	113,245	18,996,849
Accrued interest	29	5,378	226	37,976
Balance with IMF	183,280	33,696,074	183,275	30,744,446
<i>Liabilities</i>				
Counterpart to IMF allocations	112,198	20,627,530	112,322	18,841,989
IMF current account with Central Bank of Iceland	6	1,103	6	1,007
Counterpart to IMF	112,204	20,628,633	112,328	18,842,995

Note 18.3 – Foreign securities and other reserve assets

	31.12.2020	31.12.2019
Foreign securities	656,288,133	567,597,945
Foreign securities funds	1,517,473	1,325,873
Foreign derivatives	0	384,608
Foreign securities and other reserve assets, total	657,805,606	569,308,426

Changes in foreign securities and securities funds

	2020	2019
Balance at beginning of year	568,923,818	577,285,363
Purchases during the year	364,111,453	114,825,299
Sold and collected during the year	(279,899,931)	(131,937,201)
Changes in accrued interest, premiums and discounts	(3,490,982)	(1,887,141)
Unrealised value adjustments	6,791,345	6,415,025
Exchange rate difference	1,369,903	4,222,472
Balance at end of year	657,805,606	568,923,818

Note 18.4 – Non-reserve assets

Non-reserve assets consisted of a claim denominated in Danish kroner against a non-resident.

Note 19 – Claims on residents, foreign-denominated

Foreign-denominated claims on residents at the end of 2019 consisted solely of a euro-denominated account with a domestic commercial bank. The Central Bank had no foreign-denominated claims on residents at the end of 2020.

Note 20 – Monetary policy-related claims against residents

Note 20.1 – Treasury

Monetary policy-related claims against the Treasury consist solely of Treasury securities.

Note 20.2 – Deposit institutions

Monetary policy-related claims against deposit institutions consist solely of support loans.

Note 21 – Claims on non-residents, króna-denominated

Claims on non-residents, króna-denominated consist solely of housing bonds.

Note 22 – Other assets

Note 22.1 – Fixed operational assets

31.12.2020	Real estate	Liquid assets	Libraries and collections	Total
<i>Cost price and valuation</i>				
Cost price at beginning of year	4,698,232	253,862	310,567	5,262,661
Valuation at beginning of year	3,477,568			3,477,568
Merger with Financial Supervisory Authority		50,968	5	50,973
Special revaluation	(124,111)			(124,111)
Capitalised during the year	230,856	112,760		343,616
Sold and discontinued during the year		(31,655)		(31,655)
Balance at end of year	<u>8,282,545</u>	<u>385,935</u>	<u>310,572</u>	<u>8,979,052</u>
<i>Depreciation</i>				
Balance at beginning of year	787,715	162,712		950,427
Depreciation for the year	88,093	40,987		129,080
Sold and discontinued during the year		(29,445)		(29,445)
Balance at end of year	<u>875,808</u>	<u>174,254</u>	<u>0</u>	<u>1,050,062</u>
Book value at beginning of year	<u>7,388,085</u>	<u>91,150</u>	<u>310,567</u>	<u>7,789,802</u>
Book value at end of year	<u>7,406,737</u>	<u>211,681</u>	<u>310,572</u>	<u>7,928,990</u>
Annual depreciation rate	0-3%	10-33%	0%	

The official end-2020 property valuation of tangible operational assets was 5.9 b.kr.

The assessed end-2020 insurance value of tangible operational assets was 9.4 b.kr.

31.12.2019	Real estate	Liquid assets	Libraries and collections	Total
<i>Cost price and valuation</i>				
Cost price at beginning of year	4,698,232	230,322	247,687	5,176,241
Valuation at beginning of year	2,273,927			2,273,927
Special revaluation	1,203,641			1,203,641
Capitalised during the year		30,740		30,740
Sold and discontinued during the year		(7,200)		(7,200)
Transferred to museum			62,880	62,880
Balance at end of year	<u>8,175,800</u>	<u>253,862</u>	<u>310,567</u>	<u>8,740,229</u>
<i>Depreciation</i>				
Balance at beginning of year	712,025	143,693		855,718
Depreciation for the year	75,690	21,230		96,920
Sold and discontinued during the year	(2,211)	(2,211)		
Balance at end of year	<u>787,715</u>	<u>162,712</u>	<u>0</u>	<u>950,427</u>
Book value at beginning of year	<u>6,260,134</u>	<u>86,629</u>	<u>247,687</u>	<u>6,594,450</u>
Book value at end of year	<u>7,388,085</u>	<u>91,150</u>	<u>310,567</u>	<u>7,789,802</u>
Annual depreciation rate	0-3%	10-20%	0%	

In 2019, a gold bar was taken from the international reserves and given to the Bank's museum and numismatic collection. The official end-2019 property valuation of tangible operational

assets was 5.7 b.kr. The assessed end-2019 insurance value of tangible operational assets was 8.8 b.kr.

Note 22.2 – Software

	2020	2019
<i>Cost price</i>		
Balance at beginning of year	1,555,780	1,314,681
Merger with Financial Supervisory Authority	2,140	0
Capitalised during the year	310,349	241,099
Sold and discontinued during the year	(571,486)	0
Balance at end of year	<u>1,296,783</u>	<u>1,555,780</u>
<i>Depreciation</i>		
Balance at beginning of year	787,773	721,957
Depreciation for the year	96,898	65,816
Sold and discontinued during the year	(571,486)	0
Balance at end of year	<u>313,185</u>	<u>787,773</u>
Book value at beginning of year	<u>768,007</u>	<u>592,724</u>
Book value at end of year	<u>983,598</u>	<u>768,007</u>

The depreciation rates for software are 10-20% for the group. The group does not begin to depreciate software until it is brought into use. The new interbank system was brought into use on 23 October 2020 and is depreciated from that date onwards. The group capitalised software development work in the amount of 141.4 m.kr. in connection with the implementa-

tion of a new function in the Ark system (an electronic document publication system and collections system) in 2018-2020. The group will begin to depreciate this software development work when the new function is brought into use. It is estimated that the new Ark system function will be launched in March 2021.

Note 22.3 – Other assets

	31.12.2020	31.12.2019
Holdings in subsidiaries outside the group	680,439	975,423
Claims against subsidiaries outside the group	0	1,390,798
Shareholdings in Bank for Int'l Settlements	184,486	184,486
Payment intermediation claims	352,244	251,146
Pre-paid expenses	207,739	96,031
Accounts receivable	236,757	93,464
Income tax credit	11,061	6,226
Investment tax withheld	1,833	5,212
Other assets	32,583	65,952
Other assets, total	<u>1,707,142</u>	<u>3,068,738</u>

Holdings in subsidiaries outside the group

	2020	2019
Balance at beginning of year	975,423	4,291,083
Purchased during the year	0	757,789
Dividends	(350,000)	(4,282,055)
Share in earnings	55,016	208,606
Balance at end of year	<u>680,439</u>	<u>975,423</u>

Shareholdings in Bank for Int'l Settlements

Shareholdings in the Bank for International Settlements (BIS) are entered at cost price. The Central Bank owned 1,070 shares at the end of 2020. Each share has a nominal value of SDR 5,000. Payment has been made for 25% of the nominal value, or SDR 1,250 per share. The book value at year-end 2020 was 184.5 m.kr., and the nominal value of the portion

that has been paid is 246 m.kr. (SDR 1.3 million). The Central Bank of Iceland is obliged to pay for a subscription for capital shares to the Bank for International Settlements (BIS) upon request. 25% of the subscription has already been paid. The 75% share could come due for payment and totalled 738 m.kr. (SDR 4 million) at the end of 2020.

Income tax credit

	2020	2019
Balance at beginning of year	6,226	4,735
Calculated income tax for year	3,226	(20,347)
Income tax for payment in the coming year	0	21,838
Other items	1,609	0
Balance at end of year	<u>11,061</u>	<u>6,226</u>

Deferred tax is allocated as follows to individual balance sheet items:

	2020	2019
Tax loss carryforward	12,531	0
Fixed operational assets	(892)	6,834
Exchange rate difference	(27)	2
Accounts receivable	<u>(551)</u>	<u>(610)</u>
Income tax credit, total	<u>11,061</u>	<u>6,226</u>

Note 23 – Equity

Callable capital

“At the beginning of 2015, the Central Bank of Iceland and the Government entered into an agreement providing for callable capital for the Bank. With the agreement, the Treasury pledges, based on the authority contained in the National Budget, to contribute capital to the Central Bank in the form of marketable assets if the Bank calls in such capital so as to satisfy the minimum requirement for paid-in capital. The total amount of callable capital was 58.3 b.kr. at the end of 2019. With the entry into force of the new Act on the Central Bank of Iceland, no. 92/2019, on 1 January 2020, the callable capital declined by 1.1 b.kr., to 57.2 b.kr. The outstanding balance of callable capital shall be written up at year-end to accord with the increase in the consumer price index.”

Value adjustment reserve and transfer to the Treasury

The Bank's profit from the prior fiscal year, adjusted for unrealised calculated revenues and expenses, shall revert to the Treasury to the extent that it is not used to strengthen the Bank's capital position. The Bank is authorised to keep separate accounts in the equity accounts for unrealised revenues and expenses. The Bank has such an account, called the Value adjustment reserve, in its equity accounts. Unrealised revenues due to the share in the profits of subsidiaries in excess of dividends received are recognised in the equity item Unrealised share in profit of associates.

The main objective of maintaining the value adjustment reserve is to ensure that only realised gains are used as the basis for the

transfer to the Treasury or for the strengthening of the Bank's equity. Unrealised profits are entered to the value adjustment reserve. Unrealised losses in excess of previously entered unrealised gains are used to reduce the profit available for disposition.

The revaluation consists of updated market prices and currency exchange rate movements, and it extends to financial assets and liabilities, derivatives, and gold. Financial instruments denominated in domestic and foreign currencies are appraised individually.

Both realised and unrealised gains are recognised in the profit and loss account. Contributions to the value adjustment reserve consist of the difference between cost price and recorded market price. Both because of systemic changes and because there was no balance in the valuation adjustment reserve at the end of 2017, it was decided that the cost price should reflect the market price as of 31 December 2017.

The value adjustment reserve specifies as follows:

	2020	2019
Balance at beginning of year	55,126,282	42,255,199
Unrealised value adjustment of foreign securities	8,823,313	6,523,949
Value adjustment of domestic securities	291,187	93,987
Exchange rate difference on foreign assets	9,499,853	22,053,540
Exchange rate difference on gold	3,683,579	2,206,933
Realised during the year (transferred from value adjustment reserve to other equity)	(10,368,151)	(18,007,326)
Balance at end of year	<u>67,056,063</u>	<u>55,126,282</u>

Disposed of the following:

	2020	2019
Profit for the year	68,253,447	22,443,617
Change in value adjustment reserve (increase)	(11,929,780)	(12,871,084)
Decrease in restricted earnings	<u>225,071</u>	<u>3,992,080</u>
	<u>56,548,737</u>	<u>13,564,613</u>

By law, the Central Bank of Iceland shall be financially strong. In order to ensure that this goal is met, the Bank's profit is transferred to the Treasury, to the extent that it is not used to strengthen the Bank's capital. The profit for the year according to the annual accounts is 68.3 b.kr. The value adjustment reserve increased by 11.9 b.kr., and the restricted earnings account decreased by 225 m.kr. The allocation for the year 2020 is 56.5 b.kr.

In 2020, the Bank's capital adequacy benchmark was set at 150 b.kr. The Bank's equity at the end of 2020 was 150.8 b.kr. As a result, the Central Bank will pay a dividend to the Treasury in the amount of 802.1 m.kr. before 30 April 2021, in accordance with the Act on the Central Bank of Iceland. The profit for the year in excess of the dividend payment is used to strengthen the Bank's capital.

Real estate revaluation

The Bank's real estate is designated at fair value. A fair value assessment is carried out annually. Valuation changes are entered to a separate revaluation reserve account among equity items. The revaluation reserve is reduced by an amount equivalent to the annual depreciation of the difference between the restated price and the cost price.

Restricted earnings

If the share in the earnings of a subsidiary exceeds dividends received from that company, the difference is entered as restricted earnings.

Real estate company F fasteignafélag paid a dividend in the amount of 350 m.kr. in 2020, which reduced the balance on the restricted earnings account due to that company to zero. The year-end balance in restricted earnings, in the amount of 26.9 m.kr., is due entirely to Greidsluveitan ehf.

Developments in the Bank's capital ratio

	31.12.2020	31.12.2019	31.12.2018	31.12.2017
Equity (excl. value adjustments)	143,472,039	74,440,977	51,923,012	16,612,272
Revaluation of assets	<u>7,330,069</u>	<u>7,540,925</u>	<u>6,411,632</u>	<u>5,589,826</u>
Equity	<u>150,802,108</u>	<u>81,981,902</u>	<u>58,334,644</u>	<u>22,202,098</u>
Stock figures/ratios at year-end				
Total assets	842,821,173	839,658,186	754,637,199	763,781,851
Equity (excl. value adjustment of assets)	143,472,039	74,440,977	51,923,012	16,612,272
Equity ratio	17.9%	9.8%	7.7%	2.9%

Note 24 – Issued banknotes and coin

	31.12.2020	31.12.2019
<i>Banknotes</i>		
10,000 krónur	49,942,500	42,607,500
5,000 krónur	18,826,000	19,621,000
2,000 krónur	212,000	214,000
1,000 krónur	6,415,000	6,344,000
500 krónur	1,669,750	1,730,250
Banknotes, total	<u>77,065,250</u>	<u>70,516,750</u>
<i>Coin</i>		
100 krónur	2,791,400	2,660,000
50 krónur	730,190	706,590
10 krónur	620,560	600,780
5 krónur	132,779	130,304
1 króna	121,932	119,995
Coin, total	<u>4,396,861</u>	<u>4,217,669</u>
Issued banknotes and coin, total	<u>81,462,111</u>	<u>74,734,419</u>

Note 25 – Debt to non-residents, foreign-denominated

Foreign-denominated debt to non-residents consists of deposits and the counterpart to the IMF. Note 18.2 contains an explanation of matters relating to the IMF.

Note 25.1 – Deposits

Foreign-denominated deposits with non-resident entities consist solely of euro-denominated deposits with international institutions.

Note 26 – Debt to residents, foreign-denominated

	31.12.2020	31.12.2019
Deposits – Treasury and Government institutions	214,152,243	151,502,352
Derivatives – Treasury and Government institutions	0	384,608
Deposits – Other entities	11,561	10,122
Total	<u>214,163,804</u>	<u>151,897,082</u>

Note 27 – Debt to non-residents, króna-denominated

Note 27.1 – Deposits

Non-residents' króna-denominated deposits consist entirely of deposits with international institutions.

Note 27.2 – Certificates of deposit

Króna-denominated certificates of deposit held by non-residents derive from capital account liberalisation measures.

Note 28 – Debt to domestic credit institutions, monetary policy-related

Note 28.1 – Deposits

	31.12.2020	31.12.2019
Real-time gross settlement accounts	61,544,062	50,312,801
Current accounts	115,023	131,156
Collateral accounts	4,352,781	6,710,537
Deposits, total	<u>66,011,866</u>	<u>57,154,494</u>

Note 28.2 – Minimum reserve requirements

Minimum reserve requirements consist of two parts: a fixed non-remunerated 1% reserve requirement and an average reserve requirement, also 1%, which is included with deposits under Debt to domestic credit institutions, monetary policy-related.

In the Monetary Policy Committee's 11 March 2020 statement, it was announced that the Committee had decided to lower the average reserve requirement to 0% but maintain the fixed reserve requirement at 1%.

Note 28.3 – Term deposits

	31.12.2020	31.12.2019
Seven-day term deposits	107,362,237	65,005,417
One-month term deposits	0	180,469,800
Term deposits, > 1 month	5,586,566	0
Term deposits, total	<u>112,948,802</u>	<u>245,475,217</u>

The Central Bank decided at mid-year to stop offering one-month term deposits.

A new type of term deposit with a commitment period longer than one month was introduced in order to provide collateral for payment system overdrafts.

Note 28.4 – Certificates of deposit

Certificates of deposit derive from capital account liberalisation measures.

Note 29 – Debt to residents, króna-denominated

Note 29.1 – Treasury and Government institutions

	31.12.2020	31.12.2019
Deposits	142,098,010	81,393,075
Other liabilities	191,332	247,155
Total	<u>142,289,342</u>	<u>81,640,230</u>

Note 29.2 – Other entities

	31.12.2020	31.12.2019
Deposits	2,631,228	17,616,807
Other liabilities	5,231	40,641,677
Total	<u>2,636,459</u>	<u>58,258,484</u>

Note 30 – Other liabilities

	31.12.2020	31.12.2019
Vacation pay obligation	665,716	322,087
Unpaid salaries and related expenses	50,643	14,933
Pension obligations	162,676	174,487
Accounts payable	186,329	145,506
Other liabilities	6,440	2,387
Other liabilities, total	<u>1,071,804</u>	<u>659,400</u>

Unpaid salaries and related expenses

Unpaid salaries and related expenses that are included with other liabilities consist of debt to pension funds and labour unions. Unpaid payroll tax and pay-as-you-earn tax are included with debts to the Treasury under Debt to residents, króna-denominated.

Pension obligations

According to actuarial assessments, the Central Bank of Iceland's obligations due to pension payments to former governors and their spouses and the director of the National Economic Institute, of which the Bank bore half the operational expense, totalled 162.7 m.kr. as of year-end 2020. Payments related to these obligations totalled 30.3 m.kr. in 2020 and reduce the previously entered obligation. Increases in the Bank's obligations, after adjusting for payments, totalled 18.5 m.kr. in 2020 and are expensed.

Changes during the year specify as follows:

	2020	2019
Pension obligations at beginning of year	174,487	193,522
Paid due to retirement	(30,328)	(41,462)
Change during the year	18,517	22,427
Pension obligations at end of year	<u>162,676</u>	<u>174,487</u>

Other information

Note 31 – The króna system

	31.12.2020	31.12.2019
Deposit institutions	178,960,668	319,773,074
Financial institutions	21,844	21,323,269
Treasury	142,103,288	81,393,075
Non-residents	2,493,654	2,485,748
Other entities	1,939,787	41,296,296
Payment systems	352,244	251,146
Issued banknotes and coin	81,462,111	74,734,419
Total	<u>407,333,596</u>	<u>541,257,027</u>

The table shows total term deposits and sight deposits, issued banknotes and coin, and outstanding payment system balances at the year-end.

Note 32 – Foreign exchange transactions during the year

Foreign exchange market transactions against the króna in 2020, in ISK thousands

	<i>Purchases</i>	<i>Sales</i>	<i>Total</i>
Euro (EUR)	11,702,237	(149,426,928)	(137,724,691)
US dollar (USD)	35,769	(801,138)	(765,370)
Pound sterling (GBP)	110,830	0	110,830
Danish krone (DKK)	535	0	535
Norwegian krone (NOK)	18,333	0	18,333
Total	<u>11,867,704</u>	<u>(150,228,066)</u>	<u>(138,360,362)</u>

The largest item was due to foreign exchange market intervention, in which the Bank bought currency for 11.7 b.kr. and sold it for 143.4 b.kr.

Cross-border payments by the Central Bank and its customers in 2020, in ISK thousands

	<i>Incoming payments</i>	<i>Outgoing payments</i>	<i>Total</i>
Euro (EUR)	1,577,101	(6,098,449)	(4,521,348)
US dollar (USD)	12,867	(6,325,994)	(6,313,128)
Pound sterling (GBP)	8,628	(873,644)	(865,016)
Japanese yen (JPY)	0	(567,668)	(567,668)
Danish krone (DKK)	36,893	(583,076)	(546,183)
Norwegian krone (NOK)	788	(149,854)	(149,067)
Swedish krona (SEK)	330	244	574
Swiss franc (CHF)	244,303	(354,478)	(110,176)
Canadian dollar (CAD)	132	(93,889)	(93,756)
Total	1,881,042	(15,046,809)	(13,165,766)

The table shows cross-border payments by the Central Bank and its customers, in which funds are withdrawn from króna-denominated accounts for the payments and the transaction fees.

Foreign exchange market transactions against the króna in 2019, in ISK thousands

	<i>Purchases</i>	<i>Sales</i>	<i>Total</i>
Euro (EUR)	8,625,246	(22,638,340)	(14,013,094)
US dollar (USD)	11,503	(669,671)	(658,168)
Danish krone (DKK)	53,844	0	53,844
Norwegian krone (NOK)	6	0	6
Swedish krona (SEK)	1,154	0	1,154
Total	8,691,753	(23,308,011)	(14,616,258)

Cross-border payments by the Central Bank and its customers in 2019, in ISK thousands

	<i>Incoming payments</i>	<i>Outgoing payments</i>	<i>Total</i>
Euro (EUR)	1,153,284	(4,508,627)	(3,355,343)
US dollar (USD)	363,002	(4,444,403)	(4,081,401)
Pound sterling (GBP)	52,132	(912,627)	(860,495)
Japanese yen (JPY)	0	(68,050)	(68,050)
Danish krone (DKK)	113,614	(369,849)	(256,236)
Norwegian krone (NOK)	282	(117,486)	(117,204)
Swedish krona (SEK)	10,337	9,603	19,940
Swiss franc (CHF)	194,533	(231,735)	(37,203)
Canadian dollar (CAD)	76	(100,735)	(100,659)
Total	1,887,260	(10,743,910)	(8,856,651)

Note 33 – Related parties

Related parties are the State (owner of the Central Bank of Iceland), F fasteignafélag ehf. (a subsidiary outside the group), the Governor, senior management, and the Supervisory Board.

Positions and transactions and all unrealised revenues and expenses between companies in the group are omitted from both the consolidated financial statements and this explanatory note.

Treasury

Interest income and expense vis-à-vis the Treasury specify as follows:

	2020	2019
Interest income from Treasury securities	23,276	0
Interest expense on current accounts	3,501,006	2,790,045
Interest expense on Fx-accounts	542	3,044
Interest expense on derivatives contracts	225,255	371,022
Interest expense vis-à-vis the Treasury, total	<u>3,726,802</u>	<u>3,164,111</u>
Net interest expense vis-à-vis the Treasury	<u>(3,703,527)</u>	<u>(3,164,111)</u>

Net interest-bearing assets specify as follows:

	31.12.2020	31.12.2019
Treasury bonds	7,770,361	0

Net interest-bearing debt specifies as follows:

	31.12.2020	31.12.2019
Treasury and Government institutions' deposits	142,289,342	81,640,230
Treasury FX account	214,152,243	151,502,352
Derivative contract	0	384,608
Total	<u>356,441,585</u>	<u>233,527,190</u>

Governor, senior management, and Supervisory Board

In 2020, total remuneration to the Governor, senior management, and the Supervisory Board amounted to 426 m.kr. The Governor is not remunerated for participation in boards and committees jointly operated by institutions in

the financial market or to which the Central Bank of Iceland appoints a representative by law. Total remuneration to the Governor, senior management, and the Supervisory Board in 2020 specifies as follows:

	2020	2019
<i>Governor</i>		
Ásgeir Jónsson, from 20 August 2019 onwards	25,078	9,225
Már Guðmundsson, through 19 August 2019	0	36,482
<i>Deputy Governors</i>		
Rannveig Sigurdardóttir, Monetary Policy	24,203	23,478
Gunnar Jakobsson, Financial Stability, from 1 March 2020 onwards	17,692	0
Unnur Gunnarsdóttir, Financial Supervision, from 1 January 2020 onwards	23,049	0
<i>Senior management</i>		
Directors and Acting Directors ¹	319,623	298,806
<i>Supervisory Board</i>		
Gylfi Magnússon, chair	3,804	2,808
Thórunn Guðmundsdóttir, vice-chair	2,853	2,106
Other Supervisory Board members and alternates	9,727	7,313
Total remuneration to Governor, senior management, and Supervisory Board	426,029	380,218

1. Directors as of year-end 2020: Thórarinn G. Pétursson, Director, Economics and Monetary Policy; Sturla Pálsson, Director, Markets; Haukur C. Benediktsson, Director, Financial Stability; Finnur Sveinbjörnsson, Director, Banking; Rúnar Guðmundsson, Director, Pensions and Insurance; Páll Fridriksson, Director, Markets and Business Conduct; Björk Sigurgísladóttir, Director, Compliance and Inspections; Rannveig Júníusdóttir, Director, General Secretariat; Thóra Helgadóttir, Director, Operations; Logi Ragnarsson, Director, IT and Statistics; Erla Guðmundsdóttir, Director, Finance; Íris Guðrún Ragnarsdóttir, Director, Human Resources; and Vigdís Ósk Helgadóttir, Director, Greiðsluveitan ehf.

F fasteignafélag ehf. (subsidiary outside the group)

The group conducted no business with F fasteignafélag ehf. in 2019-2020. F fasteignafélag ehf. paid the Central Bank a dividend in the amount of 350 m.kr. in 2020.

The group had a claim against F fasteignafélag ehf. in the amount of 1,382 m.kr. at the end of 2019, which F fasteignafélag ehf. paid to the group in 2020. F fasteignafélag ehf. had no claims against the group at the end of 2020 or 2019.

Note 34 – Cost analysis

	<i>Salaries and related expenses</i>	<i>Other operating expenses and depreciation</i>	<i>Service expenses</i>	<i>Joint expenses</i>	<i>Total</i>
Senior management	680,865	81,112	0	(734,351)	27,626
Monetary policy	919,285	223,240	293,474	1,241,176	2,677,175
Financial stability	447,970	24,050	0	614,392	1,086,412
Financial supervision	1,238,257	89,825	0	1,089,673	2,417,755
Support departments	1,677,373	1,207,400	39	(2,210,891)	673,922
Greiðsluveitan	182,786	103,633	243,389	0	529,808
Total	5,146,535	1,729,260	536,903	0	7,412,698

Note 35 – Financial Supervision

According to the Act on the Payment of Expenses for Official Supervision of Financial Activities, no. 99/1999, operating surpluses and losses shall be taken into account in the determination of the supervision fee. At the time of the merger with the Central Bank of Iceland on 1 January 2020, the Financial Supervisory Authority's equity totalled 690.9 m.kr. The Central Bank Financial Supervisory Authority (FSA Iceland) recorded an operating loss of 58.8 m.kr. in 2020. FSA Iceland's cumulative operating surplus was therefore 632.1 m.kr. at the end of 2020.

The cumulative operating surplus has been taken into account in the determination of supervision fees for 2021.

	2020
Supervisory revenues	2,359,005
Salaries and related expenses	(1,238,257)
Other operating expenses	(89,825)
Joint expenses	<u>(1,089,673)</u>
Operating loss for the year	<u><u>(58,750)</u></u>

Note 36 – Other matters

The global COVID-19 pandemic and the public health measures imposed in order to curb the spread of the disease have had enormous economic repercussions. In response to this situation, the Central Bank has taken a wide range of actions, including lowering interest rates, boosting domestic financial institutions' access to capital, using the international reserves to mitigate exchange rate volatility, and commencing secondary market purchases of Treasury bonds.

The Central Bank has access to loan facilities from the Bank for International Settlements in the form of securities repurchase agreements, in the amount of 400 million US dollars, or 50.8 b.kr. at the end-2020 exchange rate. The Bank did not use these facilities in 2019 or 2020.

Note 37 – Events after the financial reporting date

No events occurred after the financial reporting date that call for corrections or additions to the consolidated annual accounts for the year ended 31 December 2020.

Risk management

The Central Bank of Iceland is a public institution that, by law, has a specific role focusing primarily on monetary policy, via its interest rate decisions and the investment of the nation's international reserves. Risk in its operations is therefore of a different type than in the operation of financial institutions, although the same terminology is used. The Central Bank of Iceland's financial risk entails claims risk, liquidity risk, and market risk. Claims risk is the risk of loss due to counterparties' or issuers' inability to fulfil their financial obligations at the designated time. Claims risk comprises issuer risk/counterparty risk and settlement risk. Liquidity risk is the risk that the Central Bank will be unable to fulfil its tasks and commitments due to insufficient assets, inability to sell assets in time, or inability to

sell assets except at significant discounts. Market risk is defined as the risk of loss due to changes in the market value of financial assets and liabilities. Market risk comprises exchange rate risk, interest rate risk, and gold price risk. In addition, the Bank operates under operational risk, which is the risk of human error or the failure of internal processes and systems.

The assets side of the Central Bank's consolidated accounts consists primarily of foreign assets, which are held in the Bank's international reserves, and domestic financial assets that are either issued or guaranteed by the Treasury. The following is a statement on the main financial risk of the Central Bank, which is primarily due to the international reserves.

Note 38 – International reserves

The international reserves are managed in accordance with rules of procedure on the maintenance of the reserves, which were updated in May 2020. The rules specify the purpose and structure

of the reserves, as well as defining the outside limits for acceptable financial risk. The investment mandate, which is set on the basis of the rules, stipulates how reserve management shall be carried out.

Note 39 – Claims risk

Below is an itemisation of the Bank's international reserves, by type, credit rating, country of issuance, and issuer/counterparty.

International reserves, by issuer/counterparty

	31.12.2020	31.12.2019
Treasuries	53.1%	54.4%
Government institutions	15.2%	8.5%
Multinational institutions	8.8%	5.1%
Federal states	2.7%	0.6%
Financial institutions	0.7%	1.5%
Deposits with central banks and BIS	13.3%	24.6%
Deposits with IMF	4.1%	3.7%
Deposits with financial institutions	0.1%	0.1%
Gold	1.9%	1.4%
Total	<u>100.0%</u>	<u>100.0%</u>

Credit ratings of issuers/counterparties in international reserves

	31.12.2020	31.12.2019
AAA	67.2%	72.8%
AA+	7.3%	4.1%
AA	8.7%	14.7%
AA-	8.6%	1.3%
A+	0.0%	0.7%
A	1.0%	0.0%
A-	4.7%	4.4%
BBB+	0.5%	0.6%
BBB	0.1%	0.0%
Gold	1.9%	1.4%
Total	<u>100.0%</u>	<u>100.0%</u>

Deposits with central banks and the Bank for International Settlements in the foreign exchange reserves comprise 13% of the reserves. In general, central banks are not assigned credit ratings, and their creditworthiness is deemed to be the same as that of the sovereign. It is assumed that the Bank for International Settlements has a credit rating of AAA.

Deposits with commercial banks in the foreign exchange reserves generally account for less than 1% of the reserves and are in various currencies at various banks. The Bank attempts to keep these deposits at a minimum (counterparty risk).

International reserves, by country of issuer/counterparty

	<i>Credit rating</i>	<i>31.12.2020</i>	<i>31.12.2019</i>
US	AAA	26.5%	31.0%
Germany	AAA	23.5%	24.2%
Multinational institutions	AAA	14.0%	10.0%
France	AA	9.2%	4.5%
UK	AA-	7.8%	10.3%
Netherlands	AAA	5.3%	4.0%
Japan	A	3.3%	4.0%
Austria	AA+	2.5%	0.2%
Canada	AA+	1.7%	0.2%
Spain	A-	1.0%	0.7%
Finland	AA+	0.8%	1.9%
Sweden	AAA	0.7%	0.7%
Ireland	A+	0.6%	0.2%
Belgium	AA-	0.4%	0.7%
Denmark	AAA	0.4%	0.5%
Norway	AAA	0.3%	0.0%
China	A+	0.2%	0.2%
Bank for International Settlements (BIS) ¹	AAA	0.0%	5.5%
Luxembourg	AAA	0.0%	0.0%
Switzerland	AAA	0.0%	0.0%
Italy	BBB-	0.0%	0.2%
Gold		1.9%	1.4%
Total		<u>100.0%</u>	<u>100.0%</u>

1. The Bank for International Settlements is owned by a large number of central banks and is therefore not classified under a given country.

Note 40 – Liquidity risk

Liquidity risk is the risk that the Central Bank will be unable to fulfil its tasks and commitments due to insufficient assets, inability to sell assets in time, or inability to sell assets except at significant discounts. The vast majority of the Bank's foreign exchange reserves are invested in highly liquid securities, deposits in central banks, and deposits with the Bank for International Settlements. Highly liquid assets are defined as bonds issued by the state in the state's own currency, and deposits with the central banks in these countries/regions or the Bank for

International Settlements, denominated in US dollars or euros. Issuers of securities must have a minimum credit rating of AA in order for the securities to be classified as highly liquid assets. Highly liquid assets accounted for 53% of the Central Bank's international reserves at the end of 2020, as opposed to 64% at the end of 2019.

The following tables specify the Central Bank's total assets and liabilities, by maturity. The tables show the difference based on foreign and domestic maturities.

Outstanding balance of financial assets and liabilities, 31 December 2020

	Available for withdrawal	< 3 months	3-12 months	1-5 years	> 5 years	Total
Gold	15,403,715					15,403,715
Claims on non-residents, foreign-denominated	796,075,644	5,393,704				801,469,348
Foreign bank deposits	104,492,911	5,393,704				109,886,615
Balance with IMF	33,696,074					33,696,074
Foreign securities and other reserve assets	657,805,606					657,805,606
Non-reserve assets	81,053					81,053
Claims on residents, monetary policy-related	7,770,361	1,749,388				9,519,749
Króna-denominated claims against residents	5,808,631					5,808,631
Other assets	1,271,353				184,486	1,455,839
	<u>826,329,704</u>	<u>7,143,092</u>	<u>0</u>	<u>0</u>	<u>184,486</u>	<u>833,657,282</u>
Banknotes and coin	81,462,111					81,462,111
Debt to non-residents, foreign-denominated	30,555,938					30,555,938
Debt to residents, foreign-denominated	214,163,804					214,163,804
Debt to non-residents, króna-denominated	2,494,998				6,767,366	9,262,364
Deposits	2,494,998					2,494,998
Certificates of deposit					6,767,366	6,767,366
Debt to domestic credit institutions, monetary policy-related	66,011,866	137,436,114			7,129,263	210,577,243
Deposits	66,011,866					66,011,866
Minimum reserve requirements		24,487,312				24,487,312
Term deposits		112,948,802				112,948,802
Certificates of deposit					7,129,263	7,129,263
Debt to residents, króna-denominated	144,925,801					144,925,801
Other liabilities	6,440	236,972	665,716	162,676		1,071,804
	<u>539,620,958</u>	<u>137,673,086</u>	<u>665,716</u>	<u>162,676</u>	<u>13,896,629</u>	<u>692,019,065</u>
Net outstanding in foreign currency	<u>566,759,617</u>	<u>5,393,704</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>572,153,321</u>
Net outstanding in domestic currency	<u>(280,050,871)</u>	<u>(135,923,698)</u>	<u>(665,716)</u>	<u>(162,676)</u>	<u>(13,712,143)</u>	<u>(430,515,104)</u>
Net outstanding	<u>286,708,746</u>	<u>(130,529,994)</u>	<u>(665,716)</u>	<u>(162,676)</u>	<u>(13,712,143)</u>	<u>141,638,214</u>

Analysis of outstanding financial assets and liabilities, 31 December 2019

	Available for withdrawal	< 3 months	3-12 months	1-5 years	> 5 years	Total
Gold	11,720,136					11,720,136
Claims on non-residents, foreign-denominated	743,282,035	67,057,234				810,339,269
Foreign bank deposits	143,100,466	67,057,234				210,157,700
Balance with IMF	30,744,446					30,744,446
Foreign securities and other reserve assets	569,308,426					569,308,426
Non-reserve assets	128,697					128,697
Claims on residents, foreign-denominated	37,536					37,536
Claims on residents, króna-denominated	5,934,698					5,934,698
Other assets	2,716,043				184,486	2,900,529
	<u>763,690,448</u>	<u>67,057,234</u>	<u>0</u>	<u>0</u>	<u>184,486</u>	<u>830,932,168</u>
Banknotes and coin	74,734,419					74,734,419
Debt to non-residents, foreign-denominated	24,307,059					24,307,059
Debt to residents, foreign-denominated	151,897,082					151,897,082
Debt to non-residents, króna-denominated	2,486,891				7,516,022	10,002,913
Deposits	2,486,891					2,486,891
Certificates of deposit					7,516,022	7,516,022
Debt to domestic credit institutions, monetary policy-related	57,154,494	266,325,042			32,697,161	356,176,697
Deposits	57,154,494					57,154,494
Minimum reserve requirements		20,849,825				20,849,825
Term deposits		245,475,217				245,475,217
Certificates of deposit					32,697,161	32,697,161
Debt to residents, króna-denominated	139,898,714					139,898,714
Other liabilities	2,387	160,439	322,087	174,487		659,400
	<u>450,481,046</u>	<u>266,485,481</u>	<u>322,087</u>	<u>174,487</u>	<u>40,213,183</u>	<u>757,676,284</u>
Net outstanding in foreign currency	<u>578,835,566</u>	<u>67,057,234</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>645,892,800</u>
Net outstanding in domestic currency	<u>(265,626,164)</u>	<u>(266,485,481)</u>	<u>(322,087)</u>	<u>(174,487)</u>	<u>(40,028,697)</u>	<u>(572,636,916)</u>
Net outstanding	<u>313,209,402</u>	<u>(199,428,247)</u>	<u>(322,087)</u>	<u>(174,487)</u>	<u>(40,028,697)</u>	<u>73,255,884</u>

Note 41 – Settlement risk

Settlement risk is the risk that settlement will not take place as expected; for instance, if a counterparty does not deliver securities when the Bank has delivered payment, etc. Because of the low number of transactions, settlement risk in the international reserves is generally very limited. The largest

transactions are usually bond trades, which are not settled by the securities depository until both securities and payment are delivered; therefore, settlement risk is limited. The Bank's framework for claims risk and liquidity risk sets boundaries for settlement risk.

Note 42 – Market risk

Exchange rate risk

Exchange rate risk is the risk of loss due to changes in the exchange rate of foreign currencies vis-à-vis the Icelandic króna. Attempts are made to minimise the exchange rate risk in the Bank's international reserves at all times by keeping a portion of the assets in the same currencies and the same amounts as the Bank's and the Treasury's foreign liabilities, insofar as is

possible. The exchange rate risk exposure of the Bank's net foreign exchange assets (foreign exchange balance) is then kept in a given currency composition. The Bank may use derivatives to manage its exchange rate risk. The Central Bank's foreign exchange balance was as follows at year-end 2019 and 2020:

Currencies in financial assets and liabilities 31.12.2020

	<i>Euro</i>	<i>US dollar</i>	<i>Pound sterling</i>	<i>Yen</i>	<i>Gold and other currencies</i>	<i>Total</i>
<i>Assets</i>						
Gold					15,403,715	15,403,715
Claims on non-residents, foreign-denominated	359,655,561	317,374,001	91,281,457	27,699,601	5,458,728	801,469,348
Foreign bank deposits	77,645,399	5,586,333	1,435,056	25,007,973	211,854	109,886,615
Balance with IMF	11,029,176	13,628,462	2,698,460	2,691,628	3,648,348	33,696,074
Foreign securities and other reserve assets	270,980,986	298,159,206	87,147,941		1,517,473	657,805,606
Non-reserve assets					81,053	81,053
Other assets	108,153	24,871	5,842			138,866
Assets, total	<u>359,763,714</u>	<u>317,398,872</u>	<u>91,287,299</u>	<u>27,699,601</u>	<u>20,862,443</u>	<u>817,011,929</u>
<i>Liabilities</i>						
Debt to non-residents, foreign-denominated	16,679,333	8,343,302	1,651,989	1,647,806	2,233,508	30,555,938
Deposits	9,927,305	0	9,927,305			
Counterpart to IMF	6,752,028	8,343,302	1,651,989	1,647,806	2,233,508	20,628,633
Debt to residents, foreign-denominated	214,012,492	150,190	1,115		7	214,163,804
Other liabilities	1,229	1,564	1			2,794
Liabilities, total	<u>230,693,054</u>	<u>8,495,056</u>	<u>1,653,105</u>	<u>1,647,806</u>	<u>2,233,515</u>	<u>244,722,536</u>
Net assets	<u>129,070,660</u>	<u>308,903,816</u>	<u>89,634,194</u>	<u>26,051,795</u>	<u>18,628,928</u>	<u>572,289,393</u>

Currencies in financial assets and liabilities 31.12.2019

	<i>Euro</i>	<i>US dollar</i>	<i>Pound sterling</i>	<i>Yen</i>	<i>Gold and other currencies</i>	<i>Total</i>
<i>Assets</i>						
Gold					11,720,136	11,720,136
Claims on non-residents, foreign-denominated	296,687,691	372,611,624	100,981,453	35,192,183	4,866,318	810,339,269
Foreign bank deposits	101,092,811	67,302,953	8,821,342	32,768,469	172,125	210,157,700
Balance with IMF	9,622,599	12,951,199	2,507,311	2,423,714	3,239,623	30,744,446
Foreign securities and other reserve assets	185,972,281	292,357,472	89,652,800		1,325,873	569,308,426
Non-reserve assets					128,697	128,697
Foreign-denominated claims against residents	37,536					37,536
Other assets	48,269					48,269
Assets, total	296,735,960	372,611,624	100,981,453	35,192,183	16,586,454	822,107,674
<i>Liabilities</i>						
Debt to non-residents, foreign-denominated	11,361,668	7,937,674	1,536,708	1,485,473	1,985,536	24,307,059
Deposits	5,464,064					5,464,064
Counterpart to IMF	5,897,604	7,937,674	1,536,708	1,485,473	1,985,536	18,842,995
Debt to residents, foreign-denominated	151,753,490	142,562	1,023		7	151,897,082
Other liabilities	3,631	863	5,406		268	10,168
Liabilities, total	163,118,789	8,081,099	1,543,137	1,485,473	1,985,811	176,214,309
Net assets	133,617,171	364,530,525	99,438,316	33,706,710	14,600,643	645,893,365

Interest rate risk

Interest rate risk is the risk of loss due to changes in market interest rates. The Bank's investment strategy aims at enabling the Bank to be able to fulfil its tasks and commitments at all times. As a consequence, the Bank attempts to invest in foreign assets that are liquid and issued by reliable parties. However, returns are also considered. Interest rate risk in foreign currencies is reduced by using assets to offset liabilities.

Gold price risk

Gold is a part of the international reserves, and changes in its market price therefore constitute a risk for the Bank. Gold does not comprise a large share of the reserves, however; the Bank owns about 64,000 ounces of gold, or 1.9% of the international reserves as of 31 December 2020. The Bank did not loan gold to other financial institutions during the year.

Note 43 – Risk relating to domestic market transactions and deposits

The Bank's market transactions with domestic financial institutions are of two types: short-term collateralised loans granted by the Bank to financial institutions, and financial institutions' deposits with the Bank.

The claims risk attached to Central Bank loan facilities is negligible. Collateral accepted by the Central Bank for loan facilities includes Treasury bonds, Government-guaranteed bonds, and covered bonds. The Central Bank grants loans for short periods of time. If a counterparty is unable to repay the loan, the Bank retains the underlying collateral. The Bank always takes delivery of the collateral before granting the loan and does not

return it until the loan has been repaid. As a result, its settlement risk is negligible.

Market risk is limited. The Bank monitors the market price of collateral it accepts for loans or as payment system collateral. A haircut is always taken from the market price before the loan is granted. In case of a change in the market price of assets, the Bank may require immediate delivery of additional collateral.

The Central Bank's liquidity risk in connection with domestic market transactions and deposits is negligible, as all regular transactions with financial institutions are in Icelandic krónur.

Important accounting principles

Note 44 – Important accounting principles

Note 44.1 – Foreign currencies

Transactions in foreign currencies are entered at the exchange rate on the date the transaction takes place. Monetary assets and liabilities in foreign currencies are entered at the central exchange rate at the close of the day on the financial reporting date. Exchange rate differences that are created are recognised in the profit and loss account.

Note 44.2 – Portfolio investment

Securities are recognised at fair value, and valuation changes are recognised in the profit and loss account. All of the Bank's securities are listed on active securities exchanges. The Bank estimates the fair value of securities based on the listed price on an active securities exchange on the financial reporting date.

Note 44.3 – Interest income and expense

Interest income is recognised in the profit and loss account, using the effective interest rate method. The effective interest rate is the rate that discounts estimated future cash flows on a financial instrument over its expected life or a shorter period, as applicable, to the book value of the instrument concerned. The calculation of the effective interest rate takes account of all contractual terms and conditions applying to the financial instrument, as well as transaction costs, premia, and discounts.

The effective interest rate is determined when the financial instrument is initially recognised and is not updated.

Note 44.4 – Supervisory revenues, service revenues, and other revenues

Supervisory revenues, service revenues, and other revenues are entered when accrued. Income received during the accounting year but relating to a subsequent accounting year is expensed in the balance sheet as deferred income. Income relating to the accounting year but received after the year-end is capitalised in the balance sheet.

Note 44.5 – Entry of fees

Expenses incurred in connection with acquisition of income during the period are recognised as operating expenses. Expenses incurred during the accounting year but relating to a subsequent accounting year are capitalised in the balance sheet as prepaid expenses. Expenses relating to the accounting year but payable in a subsequent accounting year are expensed in the balance sheet as accrued expenses.

Note 44.6 – Taxation

Income tax is calculated and entered in the annual financial statements. Its calculation is based on earnings before taxes, adjusted for permanent differences between taxable earnings and earnings according to the annual accounts. The income tax rate is 20%.

Income tax payable is income tax that is estimated to become due and payable in the next year due to taxable profit for the year, plus an adjustment of income tax payable for previous years.

Deferred tax derives from the difference between balance sheet items in the tax settlement, on the one hand, and the annual accounts, on the other. The difference stems from the fact that the group's income tax base is obtained by means other than those used in the preparation of the annual accounts.

The income tax credit is assessed on the financial reporting date and is only recognised to the extent that it is likely to be used to offset taxable profit in the future.

Note 44.7 – Fixed operational assets

Assets are listed among fixed operational assets when it is likely that the economic benefits of the assets concerned will be useful to the group and when it is possible to estimate the cost due to the assets in a reliable manner. Fixed operational assets are recognised using either the cost-price method or the revaluation method.

According to the cost-price method, fixed operational assets are entered at original cost price less accumulated depreciation and impairment. The cost price of fixed operational assets consists of the purchase price and all direct costs relating to putting the assets into revenue-generating condition.

The revaluation method uses fair value on the date the fixed operational assets are revalued, less depreciation and impairment. Upward value adjustments due to revaluation are entered to the revaluation reserve account as equity. When an asset is sold, depreciated, or scrapped, the portion of the revaluation reserve account that pertains to that asset is recognised as retained earnings.

Fixed operational assets are depreciated linearly over their estimated useful life, after adjusting for their expected scrap value. Profit or loss due to the sale of assets is the difference between the sale price and the book value of the asset on the date of sale and is recognised in the profit and loss account at the time of the sale.

Note 44.8 – Intangible assets

Intangible assets are capitalised only when it is deemed likely that the economic benefits of the assets concerned will be useful to the group and when it is possible to estimate the cost associated with the assets in a reliable manner. The group's intangible assets consist solely of software. Intangible assets are depreciated linearly over their expected useful life, after adjusting for their expected scrap value. Profit or loss due to the sale of assets is the difference between the sale price and the book value of the asset on the date of sale and is recognised in the profit and loss account at the time of the sale.

Note 44.9 – Impairment of non-financial assets

On the financial reporting date, the book value of assets is estimated with a view to impairment. If there is an indication of impairment, the recoverable value of the asset is estimated so as to make it possible to determine the impairment amount (if any).

Recoverable value is either the asset's net selling price or its value in use, whichever is higher. Impairment is recognised in the profit and loss account if the book value of the asset or income-generating unit is higher than its expected recoverable value. If previously recognised impairment no longer applies, the book value of the asset is increased again, but not to a level above the original cost price or depreciated cost price if the asset has a limited useful life. Impairment of goodwill cannot be reversed.

Note 44.10 – Gold

The gold held in the Bank's international reserves is recognised as a foreign asset denominated in gold as a currency, and changes in the value of gold are recognised as exchange rate differences in the profit and loss account.

Note 44.11 – Issued banknotes and coin

Issued banknotes and coin are recognised at nominal value.

Note 44.12 – Obligations

Obligations are written up in the balance sheet if it is considered likely that the group will be faced with financial expense in the future due to a specified event or transaction and it is possible to assess the monetary amount in a reliable manner.

Presentation of profit and loss account and balance sheet

Presentation of profit and loss account

	2019
<i>Interest income</i>	
From domestic assets	367,770
From foreign assets	9,098,747
	<u>9,466,517</u>
<i>Interest expense</i>	
Interest expense on domestic liabilities	(18,047,525)
Interest expense on foreign liabilities	(609,370)
	<u>(18,656,895)</u>
Net interest expense	(9,190,378)
<i>Operating revenues</i>	
Service revenues	1,009,378
Service expenses	(513,087)
Revenues from shareholdings	45,550
Value adjustments of asset prices	6,661,396
Exchange rate gains (losses) on foreign exchange transactions	(1,846)
	<u>7,201,391</u>
Outcome before operating expenses	(1,988,987)
<i>Operating expenses</i>	
Salaries and related expenses	(2,924,664)
Other operating expenses	(1,145,835)
Expense due to banknotes and coin	(1,816)
Depreciation of property and equipment	(162,736)
	<u>(4,235,051)</u>
Effects of affiliated companies outside the group	208,606
Operating loss before tax and exchange rate difference	<u>(6,015,432)</u>
Income tax	(20,347)
Loss without exchange rate difference	<u>(6,035,779)</u>
Exchange rate difference	28,479,396
Profit for the year	<u>22,443,617</u>

Presentation of balance sheet

	2019
<i>Assets</i>	
Gold	11,720,136
Foreign assets	798,800,408
FX balance with the IMF	11,723,347
Domestic financial assets	6,048,724
Fixed operational assets	8,557,809
Other assets	2,807,761
	<u>839,658,186</u>
<i>Assets, total</i>	
<i>Equity and liabilities</i>	
<i>Equity</i>	
Capital	89,763,819
Uncalled capital	(58,262,819)
Value adjustment reserve (reserve fund)	55,126,282
Revaluation of real estate and liquid assets	7,540,925
Unrealised share in profit of associates	251,966
Other equity (negative)	(12,438,271)
	<u>81,981,902</u>
<i>Equity, total</i>	
<i>Liabilities</i>	
Banknotes and coin	74,734,419
Foreign liabilities	7,517,165
Counterpart to IMF	18,842,995
Deposits of financial institutions	74,771,301
Other deposits	281,497,157
Domestic financial liabilities	299,406,811
Pension obligations	174,487
Other liabilities	731,949
	<u>757,676,284</u>
<i>Liabilities, total</i>	
<i>Equity and liabilities</i>	
	<u>839,658,186</u>

Appendix

IX

Press releases from the Central Bank of Iceland 2020

- | No. | | No. | |
|-----|--|-----|--|
| 1 | 2 January
Financial Supervisory Authority and Central Bank of Iceland merge | 11 | 8 April
Statements by the Financial Supervision Committee, Financial Stability Committee, and Monetary Policy Committee of the Central Bank of Iceland due to the COVID-19 pandemic |
| 2 | 3 January
First meeting of the Central Bank Financial Supervision Committee | 12 | 17 April
Rules on Central Bank Facilities for Financial Undertakings amended |
| 3 | 14 January
Foreign exchange market, exchange rate developments, and international reserves 2019 | 13 | 17 April
Agreement on guarantee of credit institutions' supplemental loans to businesses |
| 4 | 5 February
Statement of the Monetary Policy Committee 5 February 2020 | 14 | 22 April
Announcement on Central Bank of Iceland purchases of Treasury bonds |
| 5 | 2 March
Current account surplus 51 b.kr. in Q4/2019 – net IIP positive by 667 b.kr. | 15 | 12 May
Central Bank and credit institutions sign agreements on bridge loans |
| 6 | 11 March
Statement of the Monetary Policy Committee 11 March 2020 | 16 | 20 May
Statement of the Monetary Policy Committee 20 May 2020 |
| 7 | 18 March
Statement of the Monetary Policy Committee 18 March 2020 | 17 | 29 May
Current account surplus 11.4 b.kr. in Q1 – IIP positive by 692 b.kr. |
| 8 | 18 March
Statement of the Financial Stability Committee 18 March 2020 | 18 | 29 May
Interest on Central Bank of Iceland certificate of deposit CB12016 |
| 9 | 23 March
Statement of the Monetary Policy Committee 23 March 2020 | 19 | 15 June
Statement by the Central Bank of Iceland on extension of the hiatus in pension funds' foreign currency purchases |
| 10 | 27 March
Central Bank to reduce one-month term deposit supply | | |

- No.
- 20 18 June
New Rules on the Foreign Exchange Market
 - 21 24 June
Support loan agreements signed
 - 22 24 June
Joint statement of the Monetary Policy Committee and the Financial Stability Committee 24 June 2020
 - 23 30 June
BIS to establish Nordic Innovation Hub Centre in Stockholm
 - 24 30 June
Announcement concerning Central Bank purchases of Treasury bonds
 - 25 1 July
Statement of the Financial Stability Committee 1 July 2020
 - 26 26 August
Statement of the Monetary Policy Committee 26 August 2020
 - 27 28 August
Special temporary collateralised lending framework for COVID support loans
 - 28 1 September
Current account surplus 7 b.kr. in Q2 – net IIP positive by 838 b.kr.
 - 29 1 September
New legislation on resolution procedures for credit institutions and investment firms
 - 30 9 September
Central Bank to begin regular programme of foreign currency sales
 - 31 18 September
Prohibition on new sales of NOVIS insurance products in Iceland
 - 32 22 September
Statement by the Central Bank of Iceland Financial Supervision Committee on assessment of risk in financial institutions' operations
 - 33 23 September
Statement of the Financial Stability Committee 23 September 2020
 - 34 30 September
Further information on the interim measure on distribution of NOVIS products
 - 35 30 September
Central Bank to continue programme of regular foreign currency sales
 - 36 30 September
Announcement concerning Central Bank purchase of Treasury bonds

- No.
- 37 7 October
Statement of the Monetary Policy Committee 7 October 2020
 - 38 9 October
New interbank system launched at the end of the week
 - 39 30 October
Central Bank to continue programme of regular foreign currency sales
 - 40 18 November
Statement of the Monetary Policy Committee 18 November 2020
 - 41 30 November
Current account deficit of 1.2 b.kr. in Q3 2020 – net international investment position positive by 33.5% of GDP
 - 42 30 November
Central Bank to continue programme of regular foreign currency sales
 - 43 16 December
Statement of the Financial Stability Committee 16 December 2020
 - 44 30 December
Central Bank to continue regular programme of foreign currency sales
 - 45 30 December
Announcement concerning Central Bank purchases of Treasury bonds

Publications by the Central Bank of Iceland 2020

In Icelandic:

Ársskýrsla 2019.
Fjármálastöðugleiki 2020, two issues.
Peningamál 2020, four issues.
Hagvísar 2020, four issues.

In English:

Annual Report 2019.
Financial Stability 2020, two issues.
Monetary Bulletin 2020, four issues.
Economic Indicators 2020, four issues.
Central Bank of Iceland Working Paper No. 83, Volatility of national account data for Iceland and other OECD countries, by Ásgeir Daniélsson (April 2020).
Central Bank of Iceland Working Paper No. 84, DYNIMO - Version III. A DSGE model of the Icelandic economy, by Stefán Thórarinnsson (December 2020).

Central Bank measures in response to COVID-19

The COVID-19 pandemic began to spread in early 2020, and governmental authorities the world over adopted a broad range of public health measures. Public gatherings were limited, curfews were imposed, travel was restricted, and the operations of many companies were scaled down significantly. The pandemic and the associated response measures caused a severe economic contraction worldwide. Iceland quickly felt the effects, particularly in the tourism sector, which weighed heavily in the domestic economy.

The Central Bank of Iceland first announced COVID-related changes in its activities on 10 March 2020, and a press release issued the following day described the Bank's first response measures. Key actions taken by the Bank were as follows:

The Bank's key interest rate was lowered by 2 percentage points in four increments: by 0.5 percentage points on 11 March, by another 0.5 percentage points on 18 March, by 0.75 percentage points on 20 May, and by 0.25 percentage points on 18 November. The aim of the rate cuts was to ease the monetary stance because of the worsening economic outlook.

On 11 March, the Bank's Monetary Policy Committee (MPC) announced the reduction of the average reserve requirement from 1% of short-term funding to 0%, and changes were made to the treatment of the fixed reserve requirement in the Bank's liquidity rules. As a result, deposit institutions' liquidity ratios increased and their liquidity position was eased by as much as 40 b.kr.

The Bank encouraged the pension funds to scale down their foreign currency purchases in response to the abrupt pandemic-induced contraction in export revenues and the potential downward pressure on the króna as a result. The pension funds stopped buying currency for foreign investments for three months starting on 17 March. They decided in June to extend that hiatus until 17 September.

On 23 March 2020, the MPC announced that the Bank would begin buying Treasury bonds in the secondary market so as to ensure that the more accommodative monetary stance would be transmitted to households and businesses. On 22 April, the Bank announced that purchases could range up to a total of 150 b.kr., they would begin in May and could range up to 20 b.kr. market value in Q2. Later, the Bank announced that secondary market bond purchases would continue, ranging up to 20 b.kr. in Q3 and another 20 b.kr. in

Q4. In Q2, purchases totalled 892 m.kr., but no bonds were bought in Q3. The Bank bought bonds for 6.7 b.kr. in Q4.

On 27 March, the Central Bank announced that it would tighten financial institutions' access to one-month term deposits with the Bank. Then, on 20 May, the MPC announced that one-month term deposits would no longer be offered.

On 8 April, in accordance with recommendations from the Bank's Financial Stability Committee (FSN), the MPC agreed to establish special temporary credit facilities in the form of collateralised loans, with a temporary expansion of the list of securities eligible as collateral for Central Bank of Iceland facilities for financial institutions. The first auction was held on 22 April 2020.

The Bank intervened in the foreign exchange market as it deemed necessary in order to mitigate short-term exchange rate volatility and lean against excessive longer-term fluctuations that could cause overshooting and subsequent correction.

On 9 September, the Bank announced its intention to begin regular sales of foreign currency in the domestic foreign exchange market, with the aim of deepening the market and improving price formation. The Bank declared its willingness to sell up to 240 million euros (40 b.kr.) in regular transactions with market makers through year-end 2020. The objective was to sell 3 million euros each business day, and announcements about the currency sales programme would be published at the end of each month. In 2020, The Bank bought currency for a total of 11.7 b.kr. and sold it for 144.4 b.kr., including 37 b.kr. through the regular sales programme.

On 18 March, the FSN announced that financial institutions' capital requirements would be eased so as to afford them greater scope to restructure distressed households' and businesses' debt while maintaining lending capacity. The countercyclical capital buffer was lowered from 2% to 0%. This measure gave credit institutions additional scope to expand their loan portfolios by 12.5%, or 350 b.kr. The Committee announced that it would not increase the countercyclical capital buffer in the next twelve months; therefore, according to the applicable rules, it would remain unchanged for at least two years, until Q1/2022. The buffer was held unchanged at the FSN's meetings in June, September, and December.

In 2019, the Bank had announced that, effective 1 April 2020, deposit institutions would be the only institutions authorised to hold deposits with the Central Bank. Because of this, deposits held by miscellaneous other financial institutions and Government institutions were re-routed into the financial system, thereby supporting the special pandemic response measures.

On 8 April, the FSN announced that it would hold the capital buffers for systemic risk and systemic importance unchanged.

Also on that date, the FSN stated that it would be appropriate to establish special temporary credit facilities in the form of collateralised loans due to uncertainty about financial institutions' liquidity.

On 17 April, the Ministry of Finance and Economic Affairs and the Central Bank announced that they had signed an agreement laying down terms and conditions for Treasury guarantees of credit institutions' supplemental loans to businesses in response to the COVID-19 pandemic.

On 12 May, the Bank announced that it had signed agreements with all of the commercial banks concerning arrangements for a Treasury guarantee on supplemental bridge loans to businesses.

The agreement between the Ministry of Finance and Economic Affairs and the Central Bank concerning the granting of Treasury guarantees vis-à-vis credit institutions in connection with COVID-19-related support loans to businesses was signed on 25 May. Thereafter, the Bank signed agreements on Treasury-guaranteed support loans with all of the commercial banks. On 24 June, the MPC and the FSN issued a joint statement announcing that the Central Bank would offer a special temporary collateralised framework for support loans, at the Bank's seven-day term deposit rate.

On 28 August, the Bank announced that it would offer commercial banks and savings banks special collateralised loans bearing a 100% Treasury guarantee, in connection with the FSN and MPC's joint announcement of 24 June.

With an announcement dated 12 March, the Central Bank Financial Supervisory Authority (FSA Iceland) urged Icelandic financial market participants to comply with the newly published recommendations from the board of the European Securities and Markets Authority (ESMA). Then, on 16 March, FSA Iceland noted that the EFTA Surveillance Authority (ESA) had decided to temporarily lower the notification thresholds of net short positions, and on 18 March, FSA Iceland expressed its support for the European Insurance and

Occupational Pensions Authority's (EIOPA) statement recommending that insurers and pension funds take various further specified actions.

On 1 April, FSA Iceland sent a circular on anti-money laundering and terrorist financing measures to obliged entities, in part due to the impact of COVID-19.

On 21 April, FSA Iceland sent pension market entities a circular containing COVID-19-related pointers on the activities of pension funds and third-pillar pension savings custodians. The circular covered business continuity, operational risk, liquidity, actuarial position, fund members' and pensioners' interests, and other information.

On 8 April, the Financial Supervision Committee (FMEN) announced that final decisions on the systemically important banks' capital requirements in the supervisory review and evaluation process (SREP) would be based on earnings reports later in the year rather than as of end-2019. Furthermore, no supervisory stress tests would be conducted at that time in connection with the SREP.

In the same statement, the Committee expressed its support for the European Banking Authority's (EBA) 25 March 2020 statement on the application of the prudential framework regarding default, forbearance, and IFRS9 in light of COVID-19 measures, and it encouraged credit institutions to use the EBA statement as a reference.

Furthermore, the FMEN expressed its support for the EBA's 31 March 2020 statement on dividends distribution, share buybacks, and variable remuneration. At the same time, the FMEN drew attention to ESMA's 12 March 2020 press release recommending that entities in the securities market take measures to ensure business continuity and comply with risk management requirements due to the COVID-19 pandemic. The Committee also drew attention to EIOPA's 2 April 2020 statement recommending that insurers temporarily suspend all dividend payments and share buybacks, owing to the uncertainty surrounding the COVID-19 pandemic.

On 22 September 2020, the Committee decided that the results of the 2019 SREP assessment concerning additional capital requirements (Pillar II-R) would remain unchanged and that developments in key risks in the commercial banks' operations would be monitored closely in the months to follow. The additional capital requirement would be reviewed if necessary, but no later than during the 2021 SREP.

The Central Bank instructed the boards of financial institutions to refrain from using their improved liquidity position and reduced capital requirements to pay dividends.

Tables



Table 1 Central Bank interest rates¹

%	<i>Bank's current accounts, nominal rates</i>	<i>Reserve requirements, nominal rates</i>	<i>Overnight lending, discount rates</i>	<i>7 day collateral lending, nominal rates</i>	<i>7 day term deposit</i>
8 February 2017	4.75	4.75	6.75	5.75	5.00
15 March 2017	4.75	4.75	6.75	5.75	5.00
17 May 2017	4.50	4.50	6.50	5.50	4.75
14 June 2017	4.25	4.25	6.25	5.25	4.50
23 August 2017	4.25	4.25	6.25	5.25	4.50
4 October 2017	4.00	4.00	6.00	5.00	4.25
15 November 2017	4.00	4.00	6.00	5.00	4.25
13 December 2017	4.00	4.00	6.00	5.00	4.25
7 February 2018	4.00	4.00	6.00	5.00	4.25
14 March 2018	4.00	4.00	6.00	5.00	4.25
16 May 2018	4.00	4.00	6.00	5.00	4.25
13 June 2018	4.00	4.00	6.00	5.00	4.25
29 August 2018	4.00	4.00	6.00	5.00	4.25
3 October 2018	4.00	4.00	6.00	5.00	4.25
7 November 2018	4.25	4.25	6.25	5.25	4.50
12 December 2018	4.25	4.25	6.25	5.25	4.50
6 February 2019	4.25	4.25	6.25	5.25	4.50
20 March 2019	4.25	4.25	6.25	5.25	4.50
22 May 2019	3.75	3.75	5.75	4.75	4.00
26 June 2019	3.50	3.50	5.50	4.50	3.75
28 August 2019	3.25	3.25	5.25	4.25	3.50
2 October 2019	3.00	3.00	5.00	4.00	3.25
6 November 2019	2.75	2.75	4.75	3.75	3.00
11 December 2019	2.75	2.75	4.75	3.75	3.00
5 February 2020	2.50	2.50	4.50	3.50	2.75
11 March 2020	2.00	2.00	4.00	3.00	2.25
18 March 2020	1.50	1.50	3.50	2.50	1.75
20 May 2020	0.75	0.75	2.75	1.75	1.00
26 August 2020	0.75	0.75	2.75	1.75	1.00
7 October 2020	0.75	0.75	2.75	1.75	1.00
18 November 2020	0.50	0.50	2.50	1.50	0.75

1. Rates on published day.

Source: Central Bank of Iceland.

Table 2 Exchange rate indices

	Narrow trade index ¹	Average exchange rate index ²			Real exchange rate ³			
		Average	Import weights	Export weights	Based on relative prices		Based on unit labour cost	
					Index	%-change	Index	%-change
2000	101.5	96.1	96.3	95.7	87.0	2.8	84.3	2.7
2001	121.4	115.4	115.1	115.3	75.7	-13.0	72.6	-13.8
2002	118.5	112.0	111.7	112.0	80.1	5.9	78.0	7.4
2003	113.4	105.3	104.8	105.4	85.4	6.5	84.7	8.6
2004	112.1	103.1	102.4	103.5	88.2	3.3	86.4	2.0
2005	100.8	92.6	91.9	93.0	100.0	13.5	100.0	15.8
2006	112.7	103.4	102.6	104.0	93.6	-6.6	96.5	-3.6
2007	110.9	100.9	99.9	101.5	98.6	5.4	101.1	4.8
2008	157.3	141.9	140.9	142.4	78.1	-20.8	72.9	-27.9
2009	210.6	191.0	190.0	191.4	63.5	-18.6	50.2	-31.1
2010	204.0	185.0	184.4	185.0	67.8	6.7	56.1	11.8
2011	204.5	183.5	183.0	183.3	68.4	0.9	59.6	6.1
2012	209.1	189.0	188.6	188.8	68.8	0.5	60.4	1.3
2013	206.5	186.3	185.9	186.1	71.4	3.8	62.5	3.6
2014	195.1	177.2	176.2	177.5	76.2	6.7	68.5	9.5
2015	189.5	176.3	175.0	177.1	79.1	3.9	74.4	8.6
2016	169.4	158.9	158.1	159.1	89.3	12.8	86.9	16.9
2017	151.2	141.1	140.6	141.1	99.9	11.9	101.6	16.8
2018	157.2	147.0	146.2	147.2	96.9	-2.9	100.4	-1.2
2019	170.6	160.0	159.1	160.4	90.4	-6.7	91.1	-9.3
2020	189.4	178.2	177.1	178.7	83.2	-7.9	82.2	-9.8

1. The index shows the average exchange rate of foreign currencies against the Icelandic króna. 31 January 2000 = 100. 2. The index shows the average exchange rate of foreign currencies against the Icelandic króna. 31 December 1994 = 100. 3. The index shows the real exchange rate of the króna in terms of relative prices and wages in Iceland's main trading partner countries. 2005 = 100.

Source: Central Bank of Iceland.

Table 3 Cash issued by the Central Bank at the year-end

	2016		2017		2018		2019		2020	
	ISK thousands	%	ISK thousands	%	ISK thousands	%	ISK thousands	%	ISK thousands	%
<i>Notes:</i>										
10,000 kr.	27,742,500	47.2	33,577,500	52.3	38,892,500	56.6	42,607,500	60.4	49,942,500	64.8
5,000 kr.	23,868,500	40.6	22,788,500	35.5	21,593,500	31.4	19,621,000	27.8	18,826,000	24.4
2,000 kr.	229,000	0.4	220,000	0.3	216,000	0.3	214,000	0.3	212,000	0.3
1,000 kr.	5,535,500	9.4	6,084,500	9.5	6,333,500	9.2	6,344,000	9.0	6,415,000	8.3
500 kr.	1,445,000	2.5	1,559,250	2.4	1,704,500	2.5	1,730,250	2.5	1,669,750	2.2
Total	58,820,500	100.0	64,229,750	100.0	68,740,000	100.0	70,516,750	100.0	77,065,250	100.0
<i>Coin:</i>										
100 kr.	2,142,300	61.1	2,335,500	61.8	2,521,200	62.5	2,660,000	63.1	2,791,400	63.5
50 kr.	592,740	16.9	638,090	16.9	679,790	16.9	706,590	16.8	730,190	16.6
10 kr.	537,410	15.3	561,430	14.9	584,190	14.5	600,780	14.2	620,560	14.1
5 kr.	120,454	3.4	125,169	3.3	128,359	3.2	130,304	3.1	132,779	3.0
1 kr.	114,539	3.3	117,455	3.1	119,599	3.0	119,995	2.8	121,932	2.8
Total	3,507,443	100.0	3,777,644	100.0	4,033,138	100.0	4,217,669	100.0	4,396,861	100.0
Total in circulation	62,327,943		68,007,394		72,773,138		74,734,419		81,462,111	

Source: Central Bank of Iceland.

Table 4 Summary of the accounts of deposit money banks¹

M.kr. at year-end	2014	2015	2016	2017	2018	2019	2020
Assets:							
Domestic assets, total	2,602,667	2,848,550	2,970,654	3,080,546	3,267,893	3,408,464	3,788,839
Cash and cash balances with Central Bank	139,069	294,599	385,056	378,700	293,870	329,923	213,018
Deposits in domestic banks	5,286	2,888	4,176	6,075	658	633	1,711
Domestic credit and marketable securities	2,314,376	2,421,376	2,461,081	2,582,965	2,861,096	2,966,389	3,451,156
Lending	1,939,689	2,025,061	2,136,566	2,357,794	2,658,135	2,734,928	3,024,495
Redeemed liabilities	237	56	32	172	121	1,208	652
Overdrafts	176,407	174,058	159,861	161,421	172,096	175,499	158,620
Bills	141	29	0	0	0	0	0
Unindexed bonds	774,870	778,048	794,271	860,684	1,020,383	1,117,854	1,482,254
Indexed bonds	783,035	815,027	902,996	989,590	1,044,223	990,083	914,227
Foreign currency bonds	362,942	349,405	320,431	366,185	423,294	471,591	518,793
Foreign currency overdrafts	21,269	20,322	34,321	29,812	34,397	25,620	21,833
Provisions	-179,212	-111,884	-75,344	-50,069	-36,380	-46,927	-71,885
Leasing contracts	40,654	47,144	51,174	49,970	49,927	49,820	46,163
Marketable bonds and bills	270,133	263,711	206,056	116,001	95,842	104,980	306,068
Equities	63,900	85,460	67,284	59,199	57,192	76,661	74,429
Derivatives	2,143	3,178	5,367	5,951	6,240	5,270	2,907
Share in associates	9,244	2,075	2,045	2,778	3,898	3,775	3,236
Share in affiliated undertakings	71,116	65,095	61,391	52,583	39,935	40,696	45,680
Other assets	61,433	59,339	51,539	51,494	62,195	61,777	71,130
Foreign assets, total	394,722	348,513	251,208	324,275	413,595	366,181	422,797
Deposits in foreign banks	91,729	99,074	56,299	77,887	107,039	63,887	85,059
Foreign credit marketable securities	297,602	243,646	188,183	233,895	293,474	285,592	317,893
Foreign lending	168,881	156,393	145,876	138,108	156,483	140,784	172,760
Provisions	-6,405	-13,793	-13,457	-4,251	-3,211	-3,238	-4,125
Marketable bonds and bills	133,415	99,227	53,590	85,778	137,139	145,433	146,996
Equities	1,709	1,818	2,175	14,260	3,063	2,613	2,262
Derivatives	1,167	1,955	2,328	7,951	8,233	10,749	15,089
Share in affiliated undertakings	1,076	26	23	16	14	9	0
Other assets	3,149	3,811	4,375	4,527	4,835	5,944	4,756
Assets, total	2,997,389	3,197,062	3,221,861	3,404,821	3,681,488	3,774,645	4,211,636
Liabilities :							
Domestic liabilities, total	2,242,985	2,256,318	2,073,439	2,146,706	2,372,585	2,479,311	2,805,621
Central Bank facilities	57,253	56,163	93	0	979	1,619	4,781
Deposits of residents, total	1,608,177	1,695,739	1,613,703	1,689,204	1,807,724	1,930,010	2,174,424
Current accounts	341,463	352,955	415,612	442,542	449,053	471,570	631,547
Current accounts in foreign currency	28,038	33,446	15,278	20,819	14,804	20,186	23,939
Sight deposits	572,154	552,629	519,050	571,616	648,178	680,973	775,859
Indexed deposits	192,856	178,820	163,112	153,826	155,922	158,538	152,911
Holiday pay accounts	9,125	10,134	11,280	12,412	13,390	14,071	14,407
Supplementary pension deposits	99,198	106,678	114,552	124,639	138,178	150,374	156,233
Other time deposits	365,343	461,077	374,818	363,351	388,199	434,298	419,527
Deposits from deposit taking corporations	17,351	4,593	1,521	1,555	2,102	2,375	2,338
Bond issue	181,652	235,043	301,852	381,545	480,400	468,361	547,725
Subordinated loans	54,239	30,590	506	194	58	170	174
Direct borrowing	229,196	145,407	65,234	396	911	1,024	1,146
Derivatives	19,002	19,641	9,774	8,853	13,299	12,715	15,546
Other liabilities	76,115	69,143	80,756	64,958	67,113	63,038	59,487
Foreign liabilities, total	150,800	282,531	508,325	600,777	683,834	667,744	745,342
Deposits from foreign deposit taking corporations	46,931	49,082	18,908	15,771	20,619	19,848	22,381
Deposits from foreign parties, other than deposit taking corporations	66,266	50,766	76,405	65,788	63,610	57,411	68,242
Derivatives	125	1,238	1,375	2,581	2,234	2,195	1,630
Bond issue	37,262	175,207	406,055	503,785	577,328	568,535	633,789

Table 4 Summary of the accounts of deposit money banks (Cont.)

	2014	2015	2016	2017	2018	2019	2020
Direct borrowing	0	6,138	5,169	12,703	19,958	19,497	19,155
Other foreign liabilities	216	100	413	148	86	258	144
Total equity and minority interest	603,604	658,214	640,097	657,338	625,069	627,590	660,673
Total liabilities and equity	2,997,389	3,197,062	3,221,861	3,404,821	3,681,488	3,774,645	4,211,636

1. The latest data are preliminary. The data only represent DMBs that are operating at each time.

Source: Central Bank of Iceland.

Table 5 Summary of the accounts of the banking system¹

M.kr. at year-end	2014	2015	2016	2017	2018	2019	2020
Foreign assets, total	924,958	1,001,522	1,067,803	1,011,728	1,150,184	1,188,425	1,239,855
Foreign credit and marketable securities	778,115	734,309	855,292	787,131	870,760	854,515	975,698
Other foreign assets	146,843	267,212	212,512	224,596	279,424	333,910	264,156
Foreign liabilities, total	239,804	313,771	547,041	628,407	709,457	682,557	766,005
Foreign bond issue	37,262	175,207	406,055	503,785	577,328	568,535	633,789
Other foreign liabilities	202,542	138,565	140,986	124,622	132,129	114,022	132,216
Domestic assets, total	2,832,981	2,792,887	2,669,461	2,778,726	2,991,456	3,064,369	3,592,171
Domestic credit and marketable securities	2,470,081	2,521,943	2,504,163	2,644,648	2,867,093	2,972,324	3,464,735
Treasury and Government institutions	371,800	309,627	206,613	125,204	36,913	38,753	248,054
Municipalities	18,931	19,626	18,365	21,387	22,220	24,422	20,360
Financial companies	82,318	51,252	46,698	58,447	82,336	97,193	123,017
Holding companies	179,256	177,708	147,368	136,909	132,652	144,847	158,001
Non-financial companies	1,102,579	1,160,414	1,201,628	1,325,845	1,487,558	1,524,874	1,506,133
Households	887,453	907,667	951,104	1,020,813	1,134,204	1,183,734	1,474,620
Non-profit institutions serving households	6,955	7,534	7,731	6,112	7,590	5,428	6,435
Provisions	-179,212	-111,884	-75,344	-50,069	-36,380	-46,927	-71,885
Other domestic assets	362,901	270,944	165,299	134,078	124,364	92,045	127,437
Domestic liabilities, total	3,518,135	3,480,637	3,190,224	3,162,047	3,432,184	3,570,237	4,066,021
Broad money and bonds (M4) ²	1,813,507	1,957,834	1,944,788	2,107,190	2,326,697	2,436,403	2,660,675
Domestic bond issue	181,652	235,043	301,852	381,545	480,400	468,361	547,725
Broad money (M3)	1,631,855	1,722,792	1,642,936	1,725,644	1,846,298	1,968,043	2,112,950
Time deposits	663,068	754,656	662,163	653,131	694,370	755,986	679,991
Money supply and sight deposits (M2)	968,788	968,135	980,772	1,072,513	1,151,927	1,212,057	1,432,959
Sight deposits	561,074	538,682	501,211	556,156	631,310	661,878	732,842
Money supply (M1)	407,713	429,453	479,561	516,358	520,618	550,179	700,118
Demand deposits	363,686	380,549	424,464	456,064	456,269	483,451	626,427
Notes and coin in circulation	44,028	48,904	55,097	60,294	64,349	66,728	73,691
Other domestic liabilities	1,704,628	1,522,803	1,245,436	1,054,857	1,105,486	1,133,834	1,405,346
Equity	678,631	736,973	684,165	679,540	683,403	709,571	811,530
Other domestic liabilities n.i.e.	1,025,997	785,830	561,271	375,317	422,083	424,263	593,816
Liabilities and equity, total	3,757,939	3,794,408	3,737,265	3,790,454	4,141,640	4,252,794	4,832,026

1. The latest data is preliminary. The data only represents DMBs that are operating at each time.

2. The money supply compilations include the deposits of all entities other than the Central Bank, deposit-taking institutions, the Treasury, and non-residents.

Source: Central Bank of Iceland.

Table 6 Liquidity and reserve ratios in %¹

<i>Effective date:</i>	<i>Total reserve requirement ratio:</i>	<i>Applied reserve requirement, fixed</i>	<i>Applied reserve requirement, averaging</i>	<i>Effective date:</i>	<i>Total reserve requirement ratio:</i>	<i>Applied reserve requirement, fixed</i>	<i>Applied reserve requirement, averaging</i>
1 March 1989	11.0		11.0	21 May 1998	4.0 (1.5) ²		4.0
1 May 1990	10.0		10.0	21 March 203	3.0 (1.0) ²		3.0
1 June 1990	7.0		7.0	21 December 203	2.0 (0.0) ³		2.0
31 October 1991	6.0		6.0	21 October 2015	4.0 (0.0) ⁴		4.0
1 January 1992	7.0		7.0	21 December 2015	2.5 (0.0) ⁴		2.5
1 November 1992	6.0		6.0	21 June 2016	2.0 (0.0) ⁴		2.0
1 December 1992	5.0		5.0	21 June 2018	2.0 (0.0) ⁵	1.0	1.0
1 November 1993	4.0 (2.5) ²		4.0	21 March 2020	1.0 (0.0)	1.0	0.0

1. Percentage of bank total deposits as of 1 June 1979, of domestic disposable funds as of 1 March 1989, and of all disposable funds as of 21 May 1998.

2. Figure in parentheses refers to the reserve ratio for bond issues and term deposits.

3. Figure in parentheses refers to the reserve ratio for deposits and bond issues with an original maturity of more than two years, and securities eligible as collateral for transactions with the Central Bank.

4. Figure in parentheses refers to the reserve ratio for deposits and bond issues with maturity more than two years, according to rules on reserves ratio no. 870 from 30 September 2015.

5. Change in credit institutions minimum reserve requirements according to rules on reserves ratio no. 585 from 4 June 2018.

Source: Central Bank of Iceland.

Table 7 Main interest rates announced pursuant to Article 10, Paragraph 2, and Temporary Provision III of the Act on Interest and Price Indexation, no. 38/2001

<i>2020</i>	<i>Non-indexed loans</i>	<i>Indexed loans</i>	<i>Penalty rates</i>	<i>Interest on damage claims</i>
1 January	5.05	2.90	10.75	3.37
1 February	5.05	2.90	10.75	3.37
1 March	4.95	2.90	10.50	3.30
1 April	4.90	2.90	9.50	3.27
1 May	4.04	2.40	9.50	2.69
1 June	4.00	2.30	8.75	2.67
1 July	3.50	2.00	8.75	2.34
1 August	3.50	2.00	8.75	2.34
1 September	3.50	2.00	8.75	2.34
1 October	3.50	1.95	8.75	2.34
1 November	3.50	1.95	8.75	2.34
1 December	3.50	2.00	8.50	2.34
Average 2020	4.08	2.35	9.33	2.72
Average 2019	5.67	3.32	11.73	3.78

Source: Central Bank of Iceland.

Table 8 Selected annual nominal yields of deposit money banks and penalty rates in % per annum

	<i>Non-indexed loans¹</i>		<i>Indexed loans¹</i>		<i>Penalty rates</i>		<i>Credit terms index, 12-month change³</i>
	<i>Nominal²</i>	<i>Real</i>	<i>Nominal²</i>	<i>Real</i>	<i>Nominal²</i>	<i>Real</i>	
2013	8.2	4.4	9.1	5.3	13.0	9.0	3.7
2014	7.8	6.7	6.4	5.3	13.0	11.8	1.0
2015	7.6	5.5	7.3	5.2	12.7	10.5	2.0
2016	8.3	6.0	7.5	5.3	13.4	11.1	2.1
2017	7.3	5.5	7.0	5.2	12.4	10.5	1.7
2018	6.9	3.6	8.6	5.2	12.0	8.5	3.3
2019	7.0	4.2	8.1	5.3	11.7	8.8	2.7
2020	5.8	2.2	8.3	4.6	9.3	5.6	3.5

1. Weighted average interest rate on new loans.

2. Flat interest.

3. Change in credit terms index (between January values), according to Statistics Iceland.

Source: Central Bank of Iceland.

Table 9 Balance sheet of the Central Bank of Iceland¹

M.kr.	Year-end					
	2014	2015	2016	2017	2018	2019
Assets:	957,277	948,340	900,649	764,530	755,189	840,240
Foreign assets	530,236	653,009	816,596	687,452	736,589	822,244
Gold	9,598	8,790	8,310	8,732	9,576	11,720
SDR	1,014	20,072	16,963	16,674	18,249	19,021
Currency balance with the IMF	3,447	3,369	10,596	10,389	11,314	11,723
Foreign deposits	35,375	129,809	111,841	96,728	119,095	210,158
Foreign securities	480,514	490,663	667,109	553,236	577,285	568,924
Other reserve assets	104	120	938	837	606	385
Other foreign assets	184	184	839	856	464	313
Domestic assets	427,041	295,331	84,053	77,077	18,600	17,996
Deposit money banks	57,048	55,993	162	78	0	38
Collateral loans	0	0	0	0	0	0
Overnight loans	0	0	0	0	0	0
Other claims in foreign currency	57,048	55,993	162	78	0	38
Other financial institutions	2,342	2,154	2,267	6,168	5,996	5,935
Listed securities	2,342	2,154	2,267	6,168	5,996	5,935
Central government	153,362	98,413	40,815	55,516	0	0
Listed securities	7,374	7,357	12,060	55,516	0	0
Bonds receivable	145,989	91,056	28,755	0	0	0
Other sectors	209,728	134,187	36,183	9,195	5,478	3,600
Sundry accounts	138	7,644	295	334	470	444
Equity holdings	30,053	11,682	35,889	8,861	5,007	1,773
Securities	179,537	114,862	0	0	0	1,382
Properties	4,202	4,152	4,102	5,441	6,260	7,388
Other asstes	358	433	524	681	866	1,035
Liabilities and Capital:	957,277	948,340	900,649	764,530	755,189	840,240
Foreign liabilities	89,004	37,378	43,885	40,334	45,581	34,310
Short term	24,597	17,223	2,893	590	3,038	7,951
Long term	43,786	0	23,961	23,046	24,357	7,516
IMF SDR allocation	20,621	20,156	17,030	16,698	18,186	18,843
Domestic liabilities	793,247	832,202	812,697	701,994	651,274	723,948
Notes and coin	49,955	55,671	62,328	68,007	72,773	74,734
Deposit money banks	133,546	288,064	377,922	371,184	285,633	352,465
Sight deposits	31,372	48,254	44,762	79,678	72,454	57,154
Time deposits	100,602	239,064	283,537	277,441	200,789	262,619
Certificates of deposit	0	0	48,451	13,526	11,818	32,692
Other claims	0	1	2	0	0	0
Sight deposits in foreign currency	1,572	744	1,170	538	573	0
Other financial institutions	65,070	53,236	77,824	93,005	95,467	61,519
Sight deposits	36,072	31,753	70,815	80,984	77,131	57,807
Time deposits	5,059	3,015	7,010	12,021	18,307	3,706
Certificates of deposit	0	0	0	0	30	5
Sight deposits in foreign currency	13,909	8,414	0	0	0	0
Time deposits in foreign currency	10,030	10,054	0	0	0	0
Central government	514,372	392,458	255,995	160,473	194,975	233,428
Treasury current accounts	143,215	89,054	66,379	76,281	104,833	70,153
Government institutions, current accounts	2,735	1,732	2,085	1,107	1,077	80
Treasury sight deposits in foreign currency	360,885	301,344	184,917	81,148	86,583	151,458
Governm. institutions foreign exch. deposits	0	0	454	498	532	44
Treasury time deposits in foreign currency	7,452	0	0	0	0	0
Other claims	84	328	2,160	1,438	1,950	11,693
Other liabilities	30,304	42,774	38,628	9,324	2,425	1,802
Capital and reserves	75,027	78,760	44,067	22,202	58,335	81,982

1. Based on the Central Bank of Iceland annual accounts.

Month-end 2020

January	February	March	April	May	June	July	August	September	October	November	December
853,686	874,969	967,590	990,908	927,572	1,030,430	985,526	993,828	964,200	948,199	887,553	843,515
835,149	855,573	947,830	971,600	907,515	1,009,439	965,102	973,394	942,773	928,469	863,948	817,058
12,427	13,132	14,475	15,993	14,925	15,646	16,975	17,256	16,662	16,824	14,980	15,404
19,285	19,696	21,957	22,707	21,083	21,628	21,610	22,163	22,123	22,520	21,522	20,861
11,885	12,127	13,520	13,983	12,974	13,310	13,299	13,638	13,613	13,858	13,242	12,835
196,661	182,301	174,947	190,919	180,906	189,510	140,227	121,640	92,369	105,819	101,291	109,887
594,249	627,687	722,245	727,327	673,967	768,685	772,706	798,409	797,720	769,162	712,628	657,806
327	334	376	380	364	375	0	0	0	0	0	0
314	296	309	291	3,296	285	285	288	287	287	286	266
18,538	19,396	19,760	19,307	20,057	20,991	20,424	20,434	21,426	19,730	23,606	26,457
0	0	0	180	180	255	0	0	968	1,218	1,429	1,749
0	0	0	180	180	180	0	0	968	1,218	1,429	1,749
0	0	0	0	0	75	0	0	0	0	0	0
0	0	0	0	0	0	0	0	0	0	0	0
6,008	6,062	6,132	6,178	6,297	6,306	6,269	6,310	6,230	6,091	5,941	5,809
6,008	6,062	6,132	6,178	6,297	6,306	6,269	6,310	6,230	6,091	5,941	5,809
0	0	0	0	447	930	932	924	927	887	4,746	7,770
0	0	0	0	447	930	932	924	927	887	4,746	7,770
0	0	0	0	0	0	0	0	0	0	0	0
4,034	4,832	5,109	4,418	4,595	4,952	4,666	4,636	4,734	2,967	2,831	2,335
870	1,668	1,945	1,254	1,450	1,807	1,521	1,491	1,590	1,188	1,058	807
1,773	1,773	1,773	1,773	1,773	1,773	1,773	1,773	1,773	1,773	1,773	1,528
1,391	1,391	1,391	1,391	1,372	1,372	1,372	1,372	1,372	6	0	0
7,388	7,388	7,366	7,366	7,366	7,362	7,362	7,362	7,346	7,346	7,346	7,407
1,107	1,114	1,153	1,166	1,172	1,187	1,194	1,201	1,221	1,221	1,313	1,387
853,686	874,969	967,590	990,908	927,572	1,030,430	985,526	993,828	964,200	948,199	887,553	843,515
34,815	34,997	37,395	38,277	36,215	36,924	37,106	41,726	41,449	42,069	40,701	39,818
8,324	8,474	8,702	8,840	8,495	8,664	8,863	12,939	12,797	13,029	12,652	12,422
7,386	7,033	6,963	6,963	6,870	6,870	6,870	6,868	6,773	6,767	6,767	6,767
19,104	19,490	21,731	22,474	20,850	21,391	21,373	21,919	21,879	22,272	21,282	20,629
724,502	728,750	739,180	734,856	729,103	812,912	768,183	755,674	730,345	703,248	676,628	652,839
72,580	72,328	72,425	72,734	74,828	76,678	77,490	77,715	78,082	78,120	79,094	81,462
378,474	394,968	381,161	343,929	346,565	337,267	356,099	302,825	335,882	270,887	235,628	210,572
53,720	57,950	69,096	84,762	108,375	58,221	62,243	50,444	90,384	85,609	47,067	66,012
291,886	303,397	278,469	228,344	208,032	248,963	263,654	222,360	215,384	155,272	159,618	137,436
32,868	33,621	33,596	30,823	30,157	30,083	30,202	30,021	30,114	30,005	28,943	7,124
0	0	0	0	0	0	0	0	0	0	0	0
0	0	0	0	0	0	0	0	0	0	0	0
61,911	58,588	68,933	27	27	27	27	27	27	27	27	27
58,201	55,855	68,927	22	22	22	22	22	22	22	22	22
3,705	2,727	0	0	0	0	0	0	0	0	0	0
5	5	5	5	5	5	5	5	5	5	5	5
0	0	0	0	0	0	0	0	0	0	0	0
0	0	0	0	0	0	0	0	0	0	0	0
209,195	200,379	213,765	315,112	304,031	395,311	331,038	371,415	312,254	350,190	357,376	356,302
51,107	44,015	38,935	132,599	130,825	138,958	113,503	147,770	89,043	123,113	129,741	134,615
10	10	30	60	10	20	50	48	58	38	23	213
152,270	155,762	174,145	179,349	170,139	253,238	214,859	220,950	220,489	224,353	217,742	214,124
44	45	50	52	49	50	29	30	30	30	29	29
0	0	0	0	0	0	0	0	0	0	0	0
5,764	547	604	3,052	3,008	3,044	2,596	2,617	2,635	2,656	9,841	7,321
2,343	2,487	2,896	3,054	3,652	3,629	3,528	3,692	4,100	4,025	4,502	4,476
94,370	111,221	191,016	217,775	162,253	180,595	180,237	196,429	192,405	202,882	170,224	150,857

Table 10 Number of entities regulated by the Financial Supervisory Authority

Categories of regulated entities at year-end	2015	2016	2017	2018	2019	2020
Subject to licence or operating under specific legislation:						
Commercial banks	4	4	4	4	4	4
Savings banks	4	4	4	4	4	4
Credit undertakings	5	5	5	5	5	4
Deposit departments of co-operative societies	1	1	1	0	0	0
Investment firms	10	10	9	9	9	9
UCITS management companies	10	10	10	9	9	9
Alternative investment fund managers ¹	0	0	0	0	0	16
Securities exchanges	1	1	1	1	1	1
Central securities depositories	1	1	2	2	2	1
Pension funds ²	26	25	22	21	21	21
Insurance companies	12	12	11	11	11	11
Insurance brokers	9	9	9	7	8	9
Entities with debt collection licenses	8	8	7	8	8	9
Payment institutions	1	1	1	1	1	2
Electronic money institutions	0	0	0	0	1	1
Currency exchange services	1	1	1	1	1	1
Guarantee funds	2	2	2	1	1	1
Registered creditors	0	0	1	1	1	0
Providers of exchange services between virtual currencies, e-money, and FIAT currencies	0	0	0	1	1	3
Total	97	95	91	87	88	106
Other regulated entities						
UCITS (not legal entities)	50	47	42	40	37	37
Investment funds (not legal entities)	53	60	60	60	54	61
Alternative investment fund managers ³	85	106	111	117	114	116
Custodians of private pension savings ⁴	8	8	8	8	8	8
Issuers of listed shares	20	21	20	23	24	23
Issuers of listed bonds	60	57	65	50	57	51
Holding companies ⁵	11	9	6	6	5	6
Financial conglomerates ⁶	0	0	0	0	0	1
Financial undertakings in winding-up proceedings	2	2	1	0	0	0
Total	386	405	404	391	387	409

1. Including nine licensed entities that are also UCITS management companies and seven registered entities, one of which is an investment firm.

2. Many pension funds are divided into divisions. There were 69 divisions at year-end 2020.

3. Previously institutional investment funds.

4. Commercial banks and savings banks. Pension funds and foreign custodians are not included.

5. Holding companies in the financial or insurance sector, or mixed holding companies.

6. Financial conglomerates in the financial or insurance sector.

Source: Central Bank of Iceland.

Table 11 Activities by foreign parties in Iceland

Number at year-end	2019	2020
Credit institutions and other financial institutions without establishments	297	303
UCITS (no. of subsidiary funds)	105 (1,115)	113 (1,291)
Investment firms with establishments	0	1
Investment firms without establishments	2,598	2,630
Central securities depositories with establishments	0	1
Insurance companies with establishments	2	2
Insurance companies without establishments	437	440
Insurance brokers with establishments	0	2
Insurance brokers and insurance agents without establishment	6.757	6.821
Payment institutions with agents (no. of agents)	3 (5)	3 (6)
Payment institutions without establishments	457	516
Electronic money institutions with distributors (no. of distributors)	3 (2)	1 (1)
Electronic money institutions without establishments	171	185
Mortgage credit without establishments	16	18
Alternative fund managers without establishments	177	205
Number of companies registered outside Europe and authorised to provide services in Iceland according to national law		
Alternative fund managers (no. of funds)	38 (88)	46 (87)

Source: Central Bank of Iceland.



ANNUAL REPORT
2020